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IN THE

Supreme Court of the United States

October Term, 1974

No. 74-1640

BETHLEHEM STEEL CORPORATION,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

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June 26, 1975

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Petitioner, Bethlehem Steel Corporation ("Bethlehem"), respectfully prays that a Writ of Certiorari issue to review the judgment of the United States Court of Claims entered in this action on February 19, 1975. The action involves a Wunderlich Act appeal from decisions of the Armed Services Board of Contract Appeals.

Opinions Below

The opinion of the Court of Claims, dated February 19, 1975 (*"Bethlehem II"*), is reported at 511 F.2d 529 (1975) and is reproduced at App. 133*. The decisions and opin-

* References to "App." are to pages of the concurrently-filed separate Appendix. The Table of Contents to the Appendix lists the page of the Appendix at which each separate opinion or order set forth therein begins.

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ions of the Armed Services Board of Contract Appeals ("ASBCA") affirmed by the judgment of the Court of Claims are reported at 71-1 BCA ¶ 8640 and 73-1 BCA ¶ 9898 and are at App. 21 and App. 42, respectively. An earlier opinion of the Court of Claims in this case, dated March 20, 1970, ("*Bethlehem I*") and reported at 423 F.2d 300 (1970), is at App. 1 and an unreported Order of the Court of Claims, dated July 1, 1971, is at App. 41.

Jurisdiction

The judgment of the Court of Claims was entered on February 19, 1975 (App. 133). Bethlehem's timely motion for rehearing and reconsideration was denied on March 28, 1975 (App. 161). This Court has jurisdiction to issue the prayed-for Writ under 28 U.S.C. § 1255(1).

Question Presented

Whether the Department of Defense, acting through an administrative committee not authorized by contract or regulation to hear or determine contract disputes, upon the *ex parte* application of a military department then in disputes clause litigation with a private contractor, has the power to require the Armed Services Board of Contract Appeals to apply, *ad hoc* and retroactively, rules-of-decision in that litigation favorable to the military department.

Constitutional Provision, Statute and Regulations Involved

The decision below determined an appeal of decisions of the ASBCA to the United States Court of Claims pursuant to the Wunderlich Act, 41 U.S.C. §§ 321-322. The decision below raises issues under the Fifth Amendment and concerns the application of certain provisions of the Armed Services Procurement Regulations, 32 C.F.R.

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§§ 3-808. The text of the Fifth Amendment, the Wunderlich Act and the relevant portions of the Armed Services Procurement Regulations are set forth at the end of this petition.

Statement of the Case

This case presents important questions concerning the fair and impartial administration of contract disputes procedures as to two contracts (NObs-3556 and NObs-3648) between Bethlehem and the Navy for the construction of five destroyers.

The Contracts

The contracts are two of seven contracts awarded by the Navy between December 15, 1952, and January 27, 1956, to four shipbuilding contractors* for the construction of a total of eighteen DD931-type destroyers. (App. 51) The facts concerning the award of the contracts and Bethlehem's performance are not in issue and are set forth in detail in the opinion of the ASBCA at App. 42.

Each of those contracts contained a provision which required the contractor to exclude from its proposed price any provision for anticipated inflation in labor and material costs which could be expected to occur during the life of the contract. In consideration for the reduced contract price resulting from such exclusion, the Government contracted to reimburse the contractor, according to an agreed formula, for such increases in labor and material costs. Such contract price "escalation" was to be an automatic adjustment, subject only to Article 6(e) of the contracts, which provided:

> "(e) The Contracting Officer may deny, in whole or in part, any upward adjustment in the contract price required under this Article if the Contracting Officer finds that such adjustment is not required, in

* Bath Iron Works, Bethlehem Steel Corporation, Ingalls Shipbuilding and Puget Sound Bridge and Dredging Co.

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whole or in part, to enable the Contractor to earn a fair and reasonable profit under this contract."

The construction and delivery of the destroyers pursuant to these contracts was completed by 1959. Bethlehem completed its deliveries to the Navy pursuant to its contracts in a timely manner, delivering the last destroyer in February 1958. There is no dispute that the destroyers delivered by Bethlehem were of "very good quality." (App. 103)

As anticipated by the parties, Bethlehem and other contractors in the DD931 program suffered significant inflationary increases in costs of labor and material. As a consequence, they submitted claims for escalation in contract prices. In January 1960 Bethlehem submitted to the Contracting Officer a claim for escalation in the contract price to cover its inflationary increases in labor and material costs. The amount of Bethlehem's claim, determined pursuant to the escalation formula in the contract, was $3,347,500 on NObs-3556 and $2,404,900 on NObs-3648. With the full escalation sought by Bethlehem, contract profit margins would have been 9.3 percent (NObs-3556) and 9.6 percent (NObs-3648).

In August 1964, four years later, the Contracting Officer refused any reimbursement whatsoever of Bethlehem's cost increases on the grounds that no escalation in contract price was required "to enable the Contractor to earn a fair and reasonable profit" within the meaning of Article 6(e) of the contracts. As matters then stood, Bethlehem would have obtained a profit on the two contracts of 3 percent (NObs-3556) and 2.3 percent (NObs-3648). In at least three out of the other five contracts, other shipbuilding contractors constructing DD931-class destroyers received escalation sufficient to recover profits of 15.2 percent, 15.32 percent and 10.1 percent. (App. 63)

Regulations Applicable to Determining "Fair and Reasonable Profit"

At the time the contract was awarded, there were no published guidelines in the Armed Services Procurement Regulations ("ASPR") as to how procurement officials were to determine what constituted a "fair and reasonable profit".*

In July, 1957, published guidelines for determining the fairness and reasonableness of profit levels were adopted by the Department of Defense. Those guidelines consisted of a number of factors which procurement officials were directed to "consider" in evaluating the proper level of profit in a Government contract. 22 F.R. 5930 (July 26, 1957). However, there was no direction or guide to Contracting Officers as to how they were to arrive at an appropriate dollar or percent-of-cost profit once they had "considered" those factors. Accordingly, the 1957 guidelines (amended in 1960) have generally been referred to as the "unweighted" guidelines.**

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* However, as the Court of Claims stated in *Bethlehem I* (App. 9):

> ". . . . Since Government officials are presumed to act properly, it is reasonable to suppose that the Pentagon would not have promulgated clauses such as Article 6(e) unless contracting officers could employ established techniques and guidelines, even if unpublished, and therefore would not act arbitrarily."

** Those were the guidelines in effect at the time of the ASBCA decision which was subsequently reviewed by the Court of Claims, in *Newport News Shipbuilding and Dry Dock Co.* v. *United States*, 374 F.2d 516 (Ct. Cl. 1967) ("*Newport News*"). *Newport News* involved a shipbuilding contract for the aircraft carrier USS Ranger which contained an escalation clause identical to that in Bethlehem's contract. The ASBCA in its initial decision in *Newport News* in 1962 had failed to apply the unweighted guidelines. The Court of Claims held, 374 F.2d at 530, the "failure to apply [profit] guidelines prescribed by authority in a regulation [to] be an error of law". Although at the time of the Court of Claims decision in *Newport News* in 1966, the unweighted guidelines at issue had been superseded by the weighted guidelines, the Court noted that their discussion "of course relates to the guidelines as they were [when the ASBCA rendered its opinion]". *Id.*

By the time of the Contracting Officer's decision in this case (August, 1964), the unweighted regulations had been superseded by more detailed, remedial guidelines. Adopted in August 1963 for immediate use, these regulations directed procurement officials to weigh the factors previously applicable according to certain standards set forth in detail in the regulations. 28 F.R. 12546, amending 32 C.F.R. Part 3, § 3-808; see "Notes and Filing Instructions" quoted at App. 156. These "weighted" guidelines were designed "to reduce the impact of subjective factors in the mind of the administering official[s]". (*Bethlehem I* App. 17; see also App. 8-9, 157) The Assistant Secretary of Defense recommended the adoption of the weighted guidelines to the Secretary of Defense as a "quantifying of existing policy" intended to force contracting officers "to give discriminating and analytical attention" to the weighting of the previous unweighted factors.* *Id.*

Decisions Below

ASBCA

The ASBCA, in August 1966, ruled that Bethlehem was restricted to a five percent profit under each of its contracts as "fair and reasonable". (App. 7) The ASBCA fixed on five percent on the theory that that was the profit to which the parties had agreed in the negotiation of the contracts. The ASBCA did not apply or advert to the weighted guidelines, then in effect and published in 32 C.F.R. ¶ 3-808, or to the superseded unweighted guidelines.

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*The memorandum reflecting that recommendation was quoted in the *Appeal of Newport News Shipbuilding and Dry Dock Co.*, dated February 9, 1971, 71-1 BCA ¶ 8705. The ASBCA stated in that appeal that the "weighted" guidelines were an implementation of historical Government profit objectives, stating:

> "The ultimate policy objectives of the Department of Defense with respect to profit, while not explicitly made public in the 1960 guidelines, were subsequently disclosed in 1963 in terms which leave no doubt that they had been present all along." (71-1 BCA ¶ 8705, at 40,455)

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Bethlehem I

Bethlehem brought this action in the Court below asserting as an error of law the ASBCA's failure to apply the weighted guidelines in effect in 1966 at the time of the ASBCA's decision. The Court, following the rationale of *Newport News,* agreed with Bethlehem:

> ". . . . Plaintiff [Bethlehem] desires to take its chances under the 'weighted guidelines method' and it has a legal right to do so." *Bethlehem I*, App. 1, 17.

The Court saw "no injustice or anomaly in applying profit limitation techniques, as the Pentagon may have amended and prescribed them from time to time, up to the date of the determination" (App. 17), and stated:

> ". . . . The involved regulations, however, when made, appeared to be remedial, meant to safeguard defense contractors against determinations as to a reasonable profit level, arbitrary, perhaps biased, or founded on 'seat-of-the-pants intuition', which contracting officers might take without proper guidelines. There is no reason to postulate an intent to withhold such safeguards from parties to then existing contracts, nothing to that effect appearing either in the contracts or the regulation." (App. 8-9)

The Navy did not argue that the weighted guidelines should not be applied to contracts entered into prior to their effective date, nor did it argue that the unweighted guidelines should apply to Bethlehem's contract.

Rather, the Navy argued that this case was an "exception" and fell "clean outside all published guidelines" because Bethlehem had not been the low bidder on NObs-3556 and NObs-3648. (App. 10-11) The Court rejected that argument, noting:

> "If defendant's postulated exemption exists, it must be a large one. The record shows that all of

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plaintiff's above named competitors in the shipbuilding industry were awarded major contracts at one time or another between World War II and 1954, when they were not the low bidders, for reasons the same as those which animated the award of NObs-3556 to plaintiff. The situation recurs so commonly in our litigation with other industries heavily dependent on defense work, that we may take judicial notice of it: a rigid adherence to procurement from the lowest bidder only is viewed in the Pentagon as gradually freezing out the competition and leading into single-source procurement." (App. 12)

Upon examination of the weighted guidelines, the Court held that the "exception" sought by the Navy was nowhere mentioned.

". . . . To put it succinctly, the alleged exception has every earmark of having originated in the active mind of defense counsel herein, not in the perhaps more rigid thinking of the Pentagon." (App. 12)

The Navy also argued that the weighted guidelines were not applicable because (i) the parties in the negotiation of the contract had agreed that a 5 percent profit was "fair and reasonable" and (ii) the "weighted" guidelines method would produce a higher, unintended result and thus be "so unfair that an exception to the method must be implied". (App. 13) The Court rejected that argument:

". . . . The contracts, however, reflect that plaintiff [Bethlehem] agreed only upon a price . . . ." (App. 13)

For the second time, the Court directed strong language at the lack of any factual or record basis for the Navy's arguments:

". . . The alleged agreement to a 5% level, in a contract that viewed prospectively could have resulted in anything from a loss to a windfall profit level,

according to its terms, must be regarded as located in defendant's counsel's eyes alone." (App. 14)

Having adjudicated Bethlehem's "legal right" to the application of the weighted guidelines, the Court went on to say:

> "If we have erred in thinking the 'Weighted guidelines method' is feasible to apply to the instant contracts, the Pentagon even now could amend or supplement its regulation, and the Board would be bound, provided no impairment of vested rights was attempted. Any amendment purporting to reaffirm the position now claimed, that officials determining a reasonable level of profit under clauses such as Article 6(e) are not subject to any published guidelines whatever in certain cases, at least would advisedly be made in light of the recent statement of the Supreme Court: '* * * a broad, roving authority, a type of administrative absolutism [is] not congenial to our law-making traditions.' *Gutknecht* v. *United States*, 396 U.S. 295, 90 S.Ct. 506, 24 L.Ed.2d 532." (App. 17-18)

ASPR Committee

Seizing upon the Court's reference to the possibility that the Pentagon might further "amend or supplement" its regulation, attorneys for the Navy sought and obtained *ex parte** a declaration by an administrative committee in

* The *ex parte* proceedings were commenced by a memorandum originating in the Office of the General Counsel of the Navy. That memorandum stated that it had been prompted by the Court of Claims decision in *Bethlehem I* and that the instructions of the ASPR Committee sought by the Navy would be presented to the ASBCA for use in contract disputes procedures with respect to Bethlehem's contract. It is clear that Navy attorneys initiated the *ex parte* proceedings and drafted the instructions (styled "Minutes") of the ASPR Committee; the Court below so found. *Bethlehem II*, App. 140. Indeed, the memorandum referred to above bears the initials of Morris Amchan, the Navy attorney immediately responsible for the conduct of the contract disputes proceedings for the Navy before the ASBCA. Bethlehem has stated in its papers in the Court below, without contravention by the Navy, that Mr. Amchan wrote the *ex parte* application and drafted the ASPR Committee "Minutes".

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the Pentagon called the Armed Services Procurement Regulation Committee (the "ASPR Committee") that the weighted guidelines were not applicable to these contracts because such application would result in an increase in the profits of the contractor beyond that "considered by the parties in the negotiation of the contract to be fair and reasonable". Navy attorneys did not advise the ASPR Committee that they had made precisely that argument to the Court of Claims in *Bethlehem I* and that the Court of Claims had rejected it as having been "located in defendant's counsel's eyes alone". (App. 14) Although Navy attorneys submitted to the ASPR Committee selected excerpts from the Court of Claims decision in *Bethlehem I*, they did not provide the Committee with a complete copy of the decision.

"Minutes" of the ASPR Committee meeting embodying its decision were drafted by Navy attorneys, were presented to the Committee and were adopted substantially verbatim.* Those "Minutes" stated that the "weighted"

*The ASPR Committee is made up of two persons appointed by the Assistant Secretary of Defense (Installations and Logistics) and two persons (one a procurement policy representative and one a legal representative) appointed by each of the military departments and by the Defense Supply Agency. The Committee's primary function is to act in an advisory capacity to the above-named Assistant Secretary on matters pertaining to the Armed Services Procurement Regulations. DoD Instruction 5126.3, December 20, 1961 (1 CCH Government Contracts Reporter ¶ 825).

The ASPR Committee has been delegated no authority to participate in contract disputes appeal procedures, either under DoD Regulations or pursuant to the disputes clause. The Secretary of Defense and the Secretaries of each of the military departments have designated the ASBCA as the only "authorized representative" to hear appeals in contract disputes proceedings (¶ 1, Armed Services Board of Contract Appeals, Part 1—Charter (4 CCH Government Contracts Reporter, ASPR A Part 1, ¶ 35, 551)) and the contract disputes clause only authorizes disputed questions to be determined by such "authorized representative". DoD Instruction 5126.3, *supra.*, establishing the ASPR Committee, does not prescribe any rules of procedure and does not by its terms provide for notice to be given to affected parties of its proceedings, for affected parties to be given an opportunity to be heard or for proceedings not to be conducted *ex parte*.

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guidelines" effected a substantive change in the standards existing at the time the contracts were entered into and were intended for the development of a profit objective for negotiation of future contracts". (As the dissent below pointed out, ". . . there is no evidence in the record to support the ASPR committee's statement that only prospective application was intended" (App. 155); there is nothing in the majority opinion to the contrary.)

The "Minutes" of the ASPR Committee directed a "deviation", *i.e.*, a non-standard procurement procedure, with respect to this contract clause, and instructed the ASBCA that the superseded unweighted guidelines should be applied in determining what level of profits was "fair and reasonable" under Article 6(e) of Bethlehem's contract.

Bethlehem was not given notice of the pendency of these collateral proceedings or opportunity to be heard.

ASBCA

The ASBCA believed itself to be "bound" by the ASPR Committee action (App. 38) and, as a result, did not pass on such questions (raised by Bethlehem) as the authority of ASPR under its charter to decide this issue absent approval of higher Department of Defense officials (App. 33) or the absence of any factual basis for the assertions of the Navy attorneys and thus for the committee's action (App. 33).*

Applying the unweighted guidelines, the ASBCA determined that Bethlehem was entitled to full escalation on NObs-3648 (resulting in a 9.6 percent profit) but restricted Bethlehem's escalation on NObs-3556 to a 6.3 percent profit level. (App. 130-131). Believing itself aggrieved on NObs-3556 by the failure of the ASBCA to apply the

* Bethlehem immediately appealed the ASBCA decision to the Court of Claims asking that Court to clarify and reaffirm its earlier opinion adjudicating Bethlehem's "legal right" to the application of the weighted guidelines. The Court of Claims declined to review the decision at that time. (App. 41)

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appropriate weighted guidelines, Bethlehem sought further review as to that contract in the Court of Claims.

Bethlehem II

In *Bethlehem II* (App. 133), the Court of Claims in a sharply-divided opinion,* approved the retroactive application of the ASPR Committee "Minutes" in Bethlehem's contract disputes proceedings. As with the ASBCA, the majority below did not go behind the Navy's assertions to review the basis for the ASPR Committee instructions.

The Court held two factors as "favoring retroactive application" of the ASPR Committee "decision": first, the "long lapse of time" between the original contract award and final disposition; second, the remedial effect of applying "a guideline regulation, any regulation" as opposed to interpreting the contract without reference to any guidelines. (App. 137-8)

The Court condemned as "not . . . entirely cricket", as "deplor[able]", and as "outrageous" the *ex parte* conduct of Navy attorneys but refused to provide Bethlehem with a remedy in order not "to prolong this already inordinately prolonged litigation, to the advantage of no one knows whom".** (App. 142-3)

The dissent below pointed out that consistent with *Bethlehem I* the only question open to the Court was whether application of the weighted guidelines was "feasible", in the sense of either "possible" or "reasonable" or "suitable".

*The Court of Claims was divided four-to-three, Judge Nichols writing the majority opinion for Judges Davis, Skelton and Kashiwa, with Judge Bennett writing a strong dissent, in which Judges Durfee and Kunzig concurred.

**It is clear to whose "advantage" the abrupt and arbitrary halt in this litigation has accrued—the Navy. Condoned in the interests of expediency are *ex parte* methods, agreed by all seven judges below to have been "outrageous", which are an anathema to notions of fundamental fair play and procedural due process. In its desire to stop this lawsuit, the majority has permitted the Navy attorneys and the ASPR Committee to engage in precisely that "administrative absolutism" verbally condemned, but effectively condoned, by the Court.

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(App. 153) The dissent noted, first, that there "can be no dispute" that it was possible to apply the weighted guidelines (App. 153)—the Navy had done so and had clearly not liked the results. Second, the application of the weighted guidelines would not be "unreasonable" when "used appropriately" to take account of the fact that Bethlehem was not the lowest bidder. (App. 153-4). Finally, the dissent dealt with each of the Navy's arguments that application of the weighted guidelines was "unsuitable", dismissing each as lacking support in the record and as having been previously rejected in *Bethlehem I*. (App. 154-7)

Reasons for Granting the Writ

The judgment sought to be reviewed holds that the Department of Defense, acting through the Armed Services Procurement Regulation Committee, upon *ex parte* application of a military department then in disputes clause litigation and without notice to the private contractor involved, has the power to require the ASBCA to apply, *ad hoc* and retroactively, rules-of-decision in that litigation favorable to the military department. In so holding, the judgment (i) is inconsistent with decisions of this Court which impose contractual and constitutional requirements of procedural regularity and basic fair play on the Government in its dealings with private parties and (ii) poses important questions and raises substantial problems in the impartial administration of disputes clause appeals before the ASBCA.

Argument

The power of the ASPR Committee, under the decision below, is "a broad, roving authority, a type of administrative absolutism not congenial to our law-making traditions". *Gutknecht* v. *United States*, 396 U.S. 295, 306 (1970). The power was invoked by the Navy here, not to

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facilitate ongoing procurement of goods or services, but to depress the recovery of moneys earned by Bethlehem under a contract which had been fully performed twelve years earlier.

Similar to the power of the Selective Service under its delinquency regulations, at issue in *Gutknecht*, such power has no statutory standard or even guidelines. The power of the ASPR Committee is exercised entirely at its own discretion — stimulated no doubt by the *ex parte* approaches of the military departments with pending contract disputes.

The decision below resolves the question presented here in a manner which is fundamentally inconsistent with decisions of this Court which are designed to protect private contractors in litigation with the Government from the retroactive application of unilateral, litigation-oriented changes in Government regulations.

1. The Government Must Conform to its Own Regulations and, During the Pendency of Litigation, May Not Apply, Ad Hoc and Retroactively, More Onerous Administrative Rules Designed To Improve Its Litigating Posture.

This Court has held in a number of decisions through the years that due process requires that the Government conform to its established regulations and procedures and not deviate therefrom on an *ad hoc* basis when it believes its interests so dictate. *Greene* v. *United States*, 376 U.S. 149 (1964); *Vitarelli* v. *Seaton*, 359 U.S. 535 (1959); *Service* v. *Dulles*, 354 U.S. 363 (1957); *United States ex rel. Accardi* v. *Shaughnessy*, 347 U.S. 260 (1954); *see also United States* v. *Heffner*, 420 F.2d 809, 811-13 (4th Cir. 1970); *Berends* v. *Butz*, 357 F.Supp. 143, 151 (D. Minn. 1973).

The Department of Defense has failed in this case to conform to its own regulations in two different ways. In the first place, the Department of Defense, acting through the ASPR Committee, has deviated on an *ad hoc* basis in a pending contract disputes litigation from its published

weighted guidelines method of evaluating the fairness and reasonableness of profit levels in negotiated contracts. In the second place, the Department of Defense, by acting through the ASPR Committee in determining the issue of what guidelines are applicable in making determinations under Article 6(e) of Bethlehem's contract, has failed to conform to its own regulations designating the ASBCA as the "authorized representative" in hearing and determining appeals in contract disputes cases "as fully and as finally" as might the Secretaries of Defense and of the military departments.

The *Greene* case is instructive on the first point. In that case Greene's employment was terminated in 1953 based on the administrative revocation of his security clearance by the Department of the Navy. Following this Court's determination that Greene's security clearance revocation had been improper, Greene sought to recover compensation for the Government's unauthorized action based on a regulation adopted in 1955. In 1960, while Greene's claim was pending, the Department of Defense "amended" its 1955 regulation so as to subject Greene's recovery to administrative discretion and to other impediments not present in the 1955 regulation. This Court held that Greene could not be forced to proceed under the amended, 1960 regulation, citing *Union Pac. Ry.* v. *Laramie Stock Yards Co.,* 231 U.S. 190, 199 (1913), to the effect that:

> ". . . 'a retrospective operation will not be given to a statute which interferes with antecedent rights . . . unless such be the "unequivocal and inflexible import of the terms, and the manifest intention of the legislature" ' ".

The *Accardi* case is instructive on the second point. There the Attorney General had included Accardi on a confidential list of "unsavory characters" whom he wished to deport, prior to the decision of a Board of Immigration Appeals

on Accardi's application for suspension of deportation proceedings. Applicable regulations then in effect delegated to the Board of Immigration Appeals such discretionary authority "as is appropriate and necessary for the disposition of the case". 8 C.F.R., 1949, § 90.3(c), cited at *United States ex rel. Accardi* v. *Shaughnessy, supra.*, 347 U.S. at 266. Accardi sought to block his deportation and offered to prove that the Board of Immigration Appeals' later denial of Accardi's application was the result of the Attorney General's instructions, but the District Court refused to accept Accardi's offer of proof. This Court reversed, holding that had the decision of the Board of Immigration Appeals resulted from the Attorney General's instruction, it would have been in error:

> "In short, as long as the regulations remain operative, the Attorney General denies himself the right to side-step the Board or dictate its decision in any manner". *United States ex rel. Accardi* v. *Shaughnessy, supra.*, 347 U.S. at 267.

This Court then noted:

> "It is important to emphasize that we are not here reviewing and reversing the ***manner*** in which discretion was exercised. If such were the case we would be discussing the evidence in the record supporting or undermining the alien's claim to discretionary relief. Rather we object to the Board's alleged *failure to exercise* its own discretion, contrary to existing valid regulations." *Id.*, at 268 (Emphasis in original.)

See also, S & E Contractors, Inc. v. *United States*, 406 U.S. 1 (1972); *United States* v. *Anthony Grace & Sons, Inc.*, 384 U.S. 424 (1966).

The decision below is inconsistent with both *Greene* and *Accardi*. Under the decisions of the Court of Claims in *Newport News* and *Bethlehem I*, Bethlehem was entitled to

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the application by the ASBCA of published DoD profit guidelines in effect at the time of ASBCA's decision in 1966, *i.e.,* the weighted guidelines. Immediately after *Bethlehem I,* and prompted by that decision, the Department of Defense, through the ASPR Committee issued an administrative instruction, considered binding by the ASBCA, that the subjective and superseded unweighted guidelines which had been discarded nine years earlier by the Department of Defense would be applied in this case in lieu of the more objective and remedial weighted guidelines. That administrative decision, issued by the ASPR Committee, was a "deviation" from published regulations of the Department of Defense, favorable to the military department—the Navy—in this litigation. And that administrative decision, on an issue in a disputes appeal pending before the ASBCA, was rendered by a committee not authorized by Department of Defense regulations to determine disputed questions in contract disputes appeals.

The change in the rules-of-decision was not effected by statute or by a general change in the overall administrative scheme. Here, the change in the rules-of-decision was a "deviation" from standard procurement practices prompted by, and intended to effect the outcome of, pending litigation. The "deviation" itself was not a more precise explication of ambiguous terminology; the "deviation" was not the extension of the regulatory scheme to areas of application not anticipated when the regulation was adopted. The "deviation" was the *ad hoc* repeal of an entire body of remedial guidelines in favor of subjective superseded guidelines.

Unlike *Accardi* there is no question that the administrative "deviation" was made to effect the outcome of this litigation. The Navy stated that it had been prompted to start the *ex parte* proceedings by the Court of Claims decision in *Bethlehem I;* the Navy claimed that the Court of Claims had invited the ASPR Committee to determine the applicability of the weighted guidelines to Bethlehem's contracts;

the Navy asserted that a higher profit would result from application of the weighted rather than unweighted guidelines; the Navy asked that the ASPR Committee instructions apply to the contract clause whose applicability was at issue only in this litigation with Bethlehem; and the Navy stated explicitly that it intended to present the ASPR Committee instructions to the ASBCA panel hearing Bethlehem's appeal.

It is clear that the Navy sought to do what it did because it believed that it had a better chance at depressing Bethlehem's recovery under the discretionary and unpredictable unweighted guidelines than it did under the objective and predictable weighted guidelines. Although application of the unweighted guidelines consistent with historical DoD profit policies should have produced the same result as application of the weighted guidelines, see *supra.* at 6n*, as indeed it did in *Newport News,* 71-1 BCA ¶ 8705 and with respect to Contract NObs-3648 below, App. 129-30, the greater subjectivity in the application of the unweighted guidelines gave the Navy the leverage of greater administrative discretion than if the weighted guidelines were applied. The Navy was successful in its strategy to the extent of $1,595,009 as to the contract still at issue in this case. Bethlehem submits that the Government cannot be permitted to manipulate published guidelines in such a manner as to achieve an improved litigating posture.

And Bethlehem submits further that protection from such arbitrary manipulation by administrative officials is precisely the objective that the weighted guidelines were designed to achieve and precisely this Court's objective in such cases as *United States ex rel Accardi* v. *Shaughnessy, supra.,* and *Greene* v. *United States, supra.* The Government simply cannot be permitted to manipulate "the law" in ways that serve its interest and quash the rights of contractors.

2. The Department of Defense May Not Finally Determine Issues in Litigation Before the ASBCA Upon Ex Parte Application of a Military Department and Without Affording the Contractor an Opportunity to Be Heard.

The "deviation" from standard procedure mandated by the ASPR Committee was obtained through an *ex parte* application of the attorneys for the Navy in this litigation. The decision of the ASPR Committee was taken by the ASBCA as "binding", not advisory. As a consequence, the Navy has not yet been forced to prove its assertions concerning the merits of the guideline substitution in an adversary hearing in which Bethlehem has had notice and an opportunity to be heard and to present its evidence.

With respect to the decision of the ASPR Committee, the Court of Claims held that such an *ex parte* approach was not improper because the ASPR Committee was a "rule-making" body to whom *ex parte* procedures were "normal". App. 144

In the context of this case, that holding is fundamentally at odds with this Court's repeated condemnations of *ex parte* procedures as inconsistent with "underlying concepts of procedural regularity and basic fair play". *Gonzales* v. *United States,* 348 U.S. 407, 412 (1955); *see also Willner* v. *Committee on Character and Fitness,* 373 U.S. 96 (1963); *Morgan* v. *United States,* 304 U.S. 1 (1938).

The "deviation" sought and obtained by Navy attorneys in the ASPR Committee proceedings was not a "rule-making" in any sense of that word. The ASPR Committee decision did not involve any particular expertise or legislative or political judgment. The ASPR Committee had to draw on no particular management or procurement background or sources in deciding that question. There was no complex "business" decision required. There was no "amendment" to existing regulations, in the sense of a clarifying, simplying or elaborating construct on existing regulations in-

tended to be widely applied. The "deviation" from standard procedures was not the product of dissatisfaction with the existing regulations arising out of experience with the weighted guidelines.

The proposal submitted to the ASPR Committee by the Navy requested a determination that the weighted guidelines not be applied retroactively to Bethlehem's contract because the effect of application "would be to increase the profit of the contractor beyond that considered by the parties in the negotiation of the contract, to be fair and reasonable." That question is the kind of question regularly and routinely adjudicated by quasi-judicial bodies or by courts themselves. And the "deviation" that was adopted by the ASPR Committee was no more than a decision of the question of whether the requested guidelines would be applied retroactively in this case. Indeed, the ASPR Committee determined one of the precise issues which was then pending before the ASBCA.

Under these circumstances the *ex parte* action of the ASPR Committee would appear to be wholly improper and the ASPR Committee action a nullity. But if any effect be ascribed to that action, the ASBCA must be given the opportunity to redetermine the issue independently, i.e., completely *de novo*. Here, the ASBCA felt itself "bound" by the ASPR Committee action and consequently did not itself inquire into the adequacy of the basis for the ASPR Committee action.

Bethlehem was entitled to participate, to offer evidence and to be heard *on the merits* of its position before the decision to change the guidelines had been administratively determined. That right derives in the first instance from its contract with the Navy wherein it is agreed that:

> "In connection with any appeal proceeding under this Article, the Contractor shall be afforded an op-

portunity to be heard and to offer evidence in support of its final appeal." (Article 33. DISPUTES.)

Bethlehem contracted for the right to be heard and to offer evidence in support of its appeals with respect to all disputed questions of fact and incidental questions of law heard before the ASBCA, *S & E Contractors, Inc.* v. *United States, supra.*, 406 U.S. at 9 n. 6; Armed Services Board of Contract Appeals, Part 1—Charter ¶ 5 (4 CCH Government Contract Reporter ¶ 35,551) ("When an appeal is taken pursuant to a disputes clause in a contract which limits appeals to disputes concerning questions of fact, the Board may nevertheless in its discretion hear, consider, and decide all questions of law necessary for the complete adjudication of the issue."), and Bethlehem was entitled to have the benefit of the administrative procedures it had bargained for. *United States* v. *Anthony Grace & Sons, Inc., supra.*, 384 U.S. at 429.

The question of what is a "fair and reasonable profit" under Article 6(e) is a disputed fact, and the issue of what guidelines are applicable in determining that disputed fact is a question involving both fact and law, but in any event a matter coming within the jurisdiction of the ASBCA.

This implies, at the very least, that Bethlehem was entitled "to be heard and to offer evidence" in an ASBCA proceeding in which the Navy was required to prove *de novo* its assertions that the "weighted" guidelines were not intended to be applied to existing contracts.

Bethlehem was entitled to a hearing as well because of the strictures of the Due Process Clause of the Fifth Amendment. Bethlehem has, in effect, been deprived of an important contractual right without essential due process requirements of notice and opportunity to be heard. See *Lynch* v. *United States*, 292 U.S. 571, 579 (1934).

("Valid contracts are property, whether the obligor be a private individual, a municipality, a State or the United States. Rights against the United States arising out of a contract with it are protected by the Fifth Amendment.")

Thus, where the Navy, in litigation with a private contractor, initiates and participates in ASPR Committee proceedings in order to obtain *ad hoc* instructions binding on the ASBCA on the particular legal and factual questions then pending before the ASBCA, the contractor must be given notice of those proceedings and an opportunity to respond to the Navy's contentions and, if any effect be given to such ASPR Committee action in later ASBCA proceedings, the issues resolved by the ASPR Committee must be redetermined *de novo* by the ASBCA.

The end result of the chain of procedural horrors discussed above is that Bethlehem has had what the Court in *Bethlehem I* characterized as a "legal right" dissolved without any administrative or judicial body deciding the merits of its side of the story.

The practice approved below is not a one-time injustice. The ASPR Committee is a continuing body whose military department members have an on-going interest in the outcome of contract disputes before the ASBCA. There is no reason to suppose the ASPR Committee and its military department members will voluntarily renounce the broad, roving authority granted by the Court below to the ASPR Committee to issue "deviations" from standard procurement procedures in pending contract disputes proceedings.

In order to preserve the orderly and impartial administration of contract disputes under the quasi-judicial structure fostered by this Court, the decision below must be reversed.

Conclusion

For the reasons stated above, petitioner Bethlehem Steel Corporation prays that a Writ of Certiorari issue to the United States Court of Claims to review its decision of February 19, 1975.

Respectfully submitted,

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Constitutional Provision, Statute and Regulations Involved

1. The Fifth Amendment to the Constitution provides:

> "No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation." (U. S. Const. Amend. V)

2. The Act of May 11, 1954, 68 Stat. 81 (The Wunderlich Act), 41 U.S.C. §§321-322, provides:

> "§321. *Limitation on pleading contract-provisions relating to finality; standards of review*
>
> "No provision of any contract entered into by the United States, relating to the finality or conclusiveness of any decision of the head of any department or agency or his duly authorized representative or board in a dispute involving a question arising under such contract, shall be pleaded in any suit now filed or to be filed as limiting judicial review of any such decision to cases where fraud by such official or his said representative or board is alleged: *Provided, however,* That any such decision shall be final and conclusive unless the same is fradulent [sic] or capricious or arbitrary or so grossly erroneous as necessarily to imply bad faith, or is not supported by substantial evidence.

"§322. *Contract-provisions making decisions final on questions of law*

"No Government contract shall contain a provision making final on a question of law the decision of any administrative official, representative, or board."

3. Relevant provisions of the Armed Services Procurement Regulations, Title 32 (Cum. Supp. as of January 1, 1960) (the "unweighted" guidelines) provide:

"§3.808-1 *General.*

"A fair and reasonable provision for profit or fee cannot be made by simply applying a certain predetermined percentage to the cost estimate or selling price of a product. Rather, the profit or fee should be first established as a dollar amount, after considering the factors set forth in this section. Therefore, where a fee is involved and it is necessary to determine the percentage relationship between the fee and the estimated cost of the contract in order to comply with administrative and statutory limitations on fees for cost-reimbursement type contracts, the percentage shall be determined only after the dollar amount of the fee has been established for negotiation purposes. [Amdt. 49, 24 F.R. 10631, Dec. 24, 1959]

"§3.808-2 *Factors for Determining Fee or Profit.*

"The factors set forth in subparagraphs (a) through (i) below should be considered in determining profit or fee in all contracts, whether for supplies or services; for construction work; or for experimental, developmental, or research work; and whether of the fixed-price type or of the cost-reimbursement type unless otherwise specified in the particular factor. All of the following factors, as set

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forth in paragraphs (a) through (i) of this section should be evaluated in the light of the basic policy set forth in §3.801-1 which provides that supplies and services shall be procured from responsible sources at fair and reasonable prices calculated to result in the lowest overall cost to the Government:

(a) *Effect of Competition.* Where competition is adequate and effective and proposals are on a firm fixed-price basis, the contracting officer normally need not consider in detail the amount of estimated profit included in a price. Where effective competition is lacking, the estimate for profit for the proposed fixed fee should be analyzed in the same manner as all other elements of price, applying the factors set forth in this section.

(b) *Degree of Risk.* (1) The degree of risk assumed by the contractor should influence the amount of profit or fee a contractor is entitled to anticipate. For example, where a portion of the risk has been shifted to the Government through cost-reimbursement or price redetermination provisions, unusual contingency provisions, or other risk-reducing measures, the amount of profit or fee should be less than where the contractor assumes all risk.

(2) Some cost-plus-a-fixed-fee contracts and task orders for research and development call for the delivery of prototypes of other "hardware." Other such contracts or task orders require only that the contractor exert its "best efforts" to deliver the required end item. Frequently this is because the contractor is not willing to assume

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the additional burden of incuring substantial cost overruns without additional fee in order to complete performance. When the contract calls for delivery of developed models in accordance with well-defined performance or design characteristics or a predetermined delivery schedule, or both, in contrast to an obligation only to exert its "best efforts" to develop and deliver such models, payment of the fee should be conditioned on performance in accordance with the contractor's obligation to deliver, and in such cases the contractor may be entitled to a larger fee both because of the risk inherent in its commitment and because of the successful completion of the work.

(c) *Nature of Work to Be Performed.* A major consideration in the determination of the amount of profit or fee, particularly in connection with experimental, developmental, or research work, is the difficulty or complexity of the work to be performed and any unusual demands of the contract, such as whether the project involves a new approach unrelated to existing equipment or only refinements on existing equipment, whether the caliber or class of engineer involved is that of an "idea-man," or whether the contractor is to be required by the contract to assign to the work unusually skilled talent.

(d) *Extent of Government Assistance.* The Department of Defense encourages its contractors to perform their contracts with the minimum of financial, facilities, or other assistance from the Government. Where extraordinary financial, facilities, or other assistance must be furnished to a contractor by the Government,

such extraordinary assistance should have a modifying effect in determining what constitutes a fair and reasonable profit or fee. (See also §3.404-3(d).)

(e) *Extent of the Contractor's Investment.* The extent of a contractor's total investment (i.e., both equity and borrowed capital) in the performance of the contract will be taken into consideration in determining the amount of the fee or profit.

(f) *Character of Contractor's Business.* Recognition must be given to the type of business normally carried on by the contractor, the complexity of manufacturing techniques, the rate of capital turnover, and the effect to each individual procurement upon such business. For example, where a contractor is engaged in an industry where the turnover of working capital is low, generally the profit objective on individual contracts is higher than in those industries where the turnover is more rapid.

(g) *Contractor's Performance.* In addition to the factors set forth in §3.101, the contractor's past and present performance should be evaluated in such areas as quality of product, quality control, scrap and spoilage, efficiency in cost control (including need for and reasonableness of cost incurred), meeting delivery schedules, timely compliance with contractual provisions, creative ability in product development giving consideration to commercial potential of product), engineering (including inventive, design simplification, and development contributions), management of subcontract programs,

and any unusual services furnished by the contractor. Where a contractor has consistently achieved excellent results in the foregoing areas in comparison with other contractors in similar circumstances, such performance merits a proportionately greater opportunity for profit or fee. Conversely, a poor record in this regard should be reflected in determining what constitutes a fair and reasonable profit or fee.

(h) *Subcontracting.* In negotiating the profit or fee, the nature and extent of any subcontracting should be considered, particularly as it bears on the contractor's performance, administrative responsibility, financial investment, and degree of risk as outlined above. The degree and nature of subcontract programs vary on a broad spectrum. While it is not possible to define precisely the exact profit or fee treatment to be accorded each situation, the general guidelines which follow will be taken into consideration. The evaluation of a contractor's subcontracting program should not consist merely of applying arbitrary percentages of profit to subcontract prices in negotiating the prime contract price. A relatively large amount of subcontracting need not make for negotiation of a lesser profit or fee—the character and circumstances of the subcontracting and the effect on the prime contractor's costs must be taken into account. Although purchased material and subcontracted work are usually properly included in the base upon which profit is computed, instances may arise in which a significant portion or portions of a contract are subcontracted in such a way that only a minimum

amount of responsibility or risk remains with the prime contractor. In such a case, the amount of fee or profit should be less than where the contractor assumes substantial risk. Of primary importance is the degree to which the subcontracting provides a better product and lower costs, with timely delivery, and in which the contractor assumes heavy managerial effort, responsibility and risk. In this connection, consideration should be given to the contractor's past and present effectiveness in offering to qualified small business concerns and to firms in labor surplus areas an opportunity to compete for subcontracts (see for example §1.707-3) and to the contractor's furnishing assistance to such concerns as they require or as the Government may specifically request. A contractor's effectiveness in furnishing such opportunity or assistance to an unusual or exceptional degree, should be given favorable consideration in determining the amount of fee or profit.

(i) *Unrealistic Estimates.* If records reveal that a contractor's actual costs are consistently lower than his estimated costs (indicating a practice of excessive estimates), and if the contractor refuses to provide what seems to be reasonable estimate of costs, a lower profit or fee should be considered." [Amdt. 49, 24 F.R. 10632, Dec. 24, 1959]

* * *

4. Relevant portions of the Armed Services Procurement Regulations, Title 32 (Cum. Supp. as of January 1, 1966) (the "weighted" guidelines) provide:

"§3.808 *Profit, including fees under cost-reimbursement type contracts.*

[28 F.R. 12555, Nov. 23, 1963]

"§3.808-1 *Policy.*

"(a) *General.* It is the policy of the Department of Defense to utilize profit to stimulate efficient contract performance. Profit generally is the basic motive of business enterprise. The Government and defense contractors should be concerned with harnessing this motive to work for more effective and economical contract performance. Negotiation of very low profits, the use of historical averages, or the automatic application of a predetermined percentage to the total estimated cost of a product, does not provide the motivation to accomplish such performance. Furthermore, low average profit rates on defense contracts overall are detrimental to the public interest. Effective national defense in a free enterprise economy requires that the best industrial capabilities be attracted to defense contracts. These capabilities will be driven away from the defense market if defense contracts are characterized by low profit opportunities. Consequently, negotiations aimed merely at reducing prices by reducing profits, with no realization of the function of profit cannot be condoned. For each contract in which profit is negotiated as a separate element of the contract price, the aim of negotiation should be to employ the profit motive so as to impel effective contract performance by which overall costs are economically controlled. To this end, the profit objective must be fitted to the circumstances of the particular procurement, giving due weight to each of the performance, risk, and other factors set forth in §§3.808-3.808-6. This will result in a wider range of profits which in many cases, will be significantly higher than previous norms.

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(b) *Contracts priced on the basis of cost analysis.* When cost analysis is performed pursuant to §3.807-2, profit considerations shall be in accordance with the objectives set forth below. As an inducement for broad reduction in defense costs, the Government should establish a profit objective for contract negotiations which will:

(1) Reward the contractor who undertakes more difficult work requiring higher skills;

(2) Allow the contractor an opportunity to earn profits commensurate with the extent of the cost risk he is willing to assume—the greater the risk assumption, the greater the profit objective established;

(3) Reward those contractors who have an excellent record of past performance and conversely penalize those contractors whose performance has been poor; and

(4) Reward contractors who provide their own facilities and financing or who have established their competence through prior development work undertaken at their own risk.

The weighted guidelines method set forth in §3.808-2 for establishing profit objectives is designed to provide reasonably precise guidance in applying these principles. This method, properly applied, will tailor profits to the circumstances of each contract in such a way that long range cost reduction objectives will be fostered, and a wider spread of profits will be achieved.

(c) *Contracts priced without cost analysis.* On many contracts and subcontracts, good pricing does

not require an examination into costs and profits. Where adequate price competition exists and in other situations where cost analysis is not required (see §3.807), fixed-price type contracts will be awarded to the lowest responsible offerors without regard to the amount of their profits. Under these circumstances, the profit which is anticipated, or in fact earned, should not be of concern to the Government. In such cases, if a low offeror earns a large profit, it should be considered the normal reward of efficiency in a competitive system and efforts should not be made to reduce such profits.

[30 F.R. 5981, Apr. 29, 1965]

"§3.808-2 *Weighted guidelines method.*

"(a) *General.* (1) The weighted guidelines method provides contracting officers with (i) a technique that will insure consideration of the relative value of the appropriate profit factors described in §3.808-4 in the establishment of a profit objective and the conduct of negotiations; and (ii) a basis for documentation of this objective, including an explanation of any significant departure from this objective in reaching a final agreement. The contracting officer's analysis of these profit factors is based on information available to him prior to negotiations. Such information is furnished in proposals, audit data, performance reports, pre-award surveys and the like. No more data on or analysis of costs should be required in the establishment of a profit objective than is required to determine if costs are reasonable. The weighted guidelines method shall be used in all contracts where cost analysis is performed except as set forth in paragraph (b) of this section.

(2) The contractor's proposal will include cost information for evaluation and a total profit figure. Contractors shall not be required to submit the details of their profit objectives but they shall not be prohibited from doing so if they desire. Elaborate and voluminous presentations are neither required nor desired and may indicate a low index of cost effectiveness, which fact itself should be taken into consideration by the contracting officer in the appropriate section of the weighted guidelines.

(3) The negotiation process does not contemplate or require agreement on either estimated cost elements or profit elements, although the details of analysis and evaluation may be discussed in the fact-finding phase of the negotiation. If the difference between the contractor's profit objective and the contracting officer's profit objective is relatively small, no discussion of individual factors may be necessary. If the negotiating parties' objectives are relatively far apart, a disclosure of weightings and rationale by both parties may be made concerning the total assigned to Input to Total Performance, Assumption of Cost Risk, Performance, Selected Factors and Special Profit Consideration. By thus developing a mutual understanding of the logic of the respective positions, an orderly progression to final agreement should result. Simultaneous, not sequential, agreement will be reached on cost, any incentive profit-sharing formulas, or limitation on profits, and price. The profit objective is a part of an overall negotiation objective which, as a going-in objective, bears a distinct relationship to the target cost objective and any proposed sharing arrangement. Since the profit is merely one of several inter-

related variables, the Government negotiator shall not complete the profit negotiation without simultaneously agreeing on the other variables. Specific agreement on the exact weights or values of the individual factors is not required and should not be attempted.

(b) *Exceptions.* (1) Under the following circumstances, other methods for establishing profit objectives may be used. Generally, it is expected that such methods will accomplish the two features of the weighted guidelines methods set forth in paragraph (a)(1) of this section. These circumstances are:

(i) Architect-engineering contracts;

(ii) Personal or professional service contracts;

(iii) Management contracts, e.g., for maintenance or operation of Government facilities;

(iv) Contracts with non-profit organizations where fees are involved;

(v) Termination settlements;

(vi) Engineering services, labor-hour, time-and-material, and overhaul contracts providing for payment on a man-hour, man-day or man-month basis, and where the contribution by the contractor constitutes the furnishing of personnel rather than the output of an integrated research, engineering, or manufacturing organization; and

(vii) Cost-reimbursement construction contracts.

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(2) Other exceptions may be made in the negotiation of contracts presenting unusual pricing situations when specifically authorized by the head of a procuring activity. Such exceptions shall be justified in writing and authorized only in situations where the weighted guidelines method is determined to be unsuitable.

(c) *Limitation.* In the event this or any other method would result in establishing a fee objective in violation of limitations established by statute or this subchapter, the maximum fee objective shall be the percentage allowed pursuant to such limitations. (See §3.405.) No local administrative ceilings on profit shall be permitted.

[30 F.R. 5981, Apr. 29, 1965]

"§3.808-3 *Profit objective.*

"(a) A profit objective is that part of the estimated contract price objective or value which, in the judgment of the contracting officer, is appropriate for the procurement being considered, covering the profit or fee element of the price objective. This objective should realistically reflect the total overall task to be performed and the requirements placed on the contractor. Prior to the negotiation of a contract, change order, or contract modification, where cost analysis is undertaken, the negotiator shall develop a profit objective. The weighted guidelines method, if applicable, shall be used for developing this profit objective. If a change or modification is of a relatively small dollar amount and is basically the same type of work as required in the basic contract, the application of the weighted guidelines method will generally result in a profit objective

similar to the profit objective in the basic contract, and therefore this basic rate may be applied to the contract change or modification. However, in cases where the change or modification calls for substantially different work, then the basic contract profit and the contractor's input to total performance may be radically changed and a detailed analysis is necessary. Also, if the dollar amount of the change or contract modification is very significant in comparison to the contract dollar amount, a detailed analysis should be made.

(b) Development of a profit objective should not begin until after a thorough (1) review of proposed contract work; (2) review of all available knowledge regarding the contractor, pursuant to Subpart I, Part 1 of this chapter, including performance, capability reports, audit data, pre-award survey reports and financial statements, as appropriate; and (3) analysis of the contractor's cost estimate and comparison with the Government's estimate or projection of cost.

[30 F.R. 5982, Apr. 29, 1965]

"§3.808-4 *Profit factors.*

"(a) The factors set forth below shall be considered in all cases in which profit is to be specifically negotiated. The weight ranges listed after each factor shall be used in all instances where the weighted guidelines method is used.

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Profit factors	*Weight ranges (percent)*
Contractor's input to total performance—	
Direct materials:	
Purchased parts	1 to 4
Subcontracted items	1 to 5
Other materials	1 to 4
Engineering labor	9 to 15
Engineering overhead	6 to 9
Manufacturing labor	5 to 9
Manufacturing overhead	4 to 7
General and administrative expenses	6 to 8
Contractor's assumption of contract cost risk	0 to 7
Type of contract.	
Reasonableness of cost estimate.	
Difficulty of contract task.	
Record of contractor's performance	−2 to +2
Management.	
Cost Efficiency.	
Reliability of cost estimates.	
Cost reduction program accomplishments.	
Value engineering accomplishments.	
Timely deliveries.	
Quality of product.	
Inventive and developmental contributions.	
Small business and labor surplus area participation.	
Selected factors	−2 to +2
Source of resources.	
Government or contractor source of financial and material resources.	
Special achievement.	
Other.	

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(b) Under the weighted guidelines method, the contracting officer shall first measure the "Contractor's Input to Total Performance" by the assignment of a profit percentage within the designated weight ranges to each element of contract cost recognized by the contracting officer. Such costs are multiplied by the specific percentages, which have been selected in accordance with §3.808-5(b), to arrive at specific dollar profits.

(c) The suggested categories under the Contractor's Input to Total Performance are similar to those on the Cost and Price Analysis Form (DD Form 633). Often, individual proposals will be in a different format; but, since these categories are broad and basic, they provide sufficient guidance to evaluate all other items of cost.

(d) Although certain classifications of acceptable cost, including travel, subsistence, facilities, test equipment, special tooling, federal manufacturers excise taxes, and royalty expenses, may have been historically excluded from the base upon which profit has been computed, they shall not be excluded when using the weighted guidelines method.

(e) After the contracting officer has computed a total dollar profit for the Contractor's Input to Total Performance, he shall divide this amount by the total recognized costs to determine the composite profit percentage for this factor. To this composite percentage, he shall then add the specific percentages assigned for cost risk, performance, and the other selected factors, to arrive at a total profit percentage. He shall then multiply the total recognized contract costs by this total profit percentage to determine the profit objective. A cardinal principle of the weighted

guidelines method is that the specific percentages assigned for cost risk, performance, and other factors are applied to total recognized costs in establishing the profit objective.

[30 F.R. 5982, Apr. 29, 1965]

"§3.808-5 *Assignment of values to specific factors.*

"(a) *General.* In making his judgment of the value of each factor, the contracting officer should be governed by the definition, description, and purpose of the factors together with considerations for evaluating them as set forth herein.

(b) *Contractor's input to total performance.* This factor is a measure of how much the contractor himself is expected to contribute to the overall effort necessary to meet the contract performance requirements in an efficient manner. This factor, which is apart from the contractor's responsibility for contract performance, takes into account what resources are necessary and what the contractor himself must do to accomplish a conversion of ideas and materials into the final product called for in the contract. This is a recognition that within a given performance output, or within a given sales dollar figure, necessary efforts on the part of individual contractors can vary widely in both value and quantity, and that the profit objective should reflect the extent and nature of the contractor's contribution to total performance. The evaluation of this factor requires an analysis of the cost content of the proposed contract as follows:

(1) *Direct materials (purchased parts, subcontracted items and other material).*

* * *

(2) *Engineering labor and manufacturing labor.*

* * *

(3) *Engineering overhead, manufacturing overhead, and general and administrative expenses.*

* * *

(c) *Contractor's assumption of contract cost risk.* (1) This factor reflects the policy of the Department of Defense to shift the risk of contract costs to the fullest extent practicable to contractors and to compensate them for the assumption of this risk. Evaluation of this risk requires a determination of (i) the degree of cost responsibility the contractor assumes, (ii) the reliability of the cost estimates in relation to the task assumed, and (iii) the chances of the contractor's success or failure. This factor is specifically limited to the risk of contract costs. Thus, such risks on the part of the contractor as reputation, losing a commercial market, risk of losing potential profits in other fields, or any risk on the part of the purchasing activity, such as the risk of not acquiring an effective weapon, are not within the scope of this factor.

(2) The first and basic determination of the degree of cost responsibility assumed by the contractor is related to the sharing of total risk of contract cost by the Government and the contractor through the selection of contract type. The extremes are a cost-plus-fixed-fee contract requiring only that the contractor use his best efforts to perform a task, and a firm fixed-price contract for a complex item. Such cost-plus-fixed-fee contract would reflect a minimum assumption of cost responsibility, whereas such firm fixed-price contract would reflect a complete assumption of cost responsibility. Therefore, in the first step of determining what value is to be

given for the contractor's assumption of contract cost risk, a zero rating shall be given to a proposed cost-plus-fixed-fee best efforts contract, and a 7-percent rating shall be given to a closely priced firm fixed-price contract for a new, complex item.

(3) The second determination is that of the reliability of the cost estimates. Sound price negotiation requires well-defined contract objectives and reliable cost estimates. Prior production experience assists the contractor in preparing reliable cost estimates on new procurements for similar equipment and does not in any way reduce his cost responsibility in a firm fixed-price contract. An excessive cost estimate reduces the possibility that the cost of performance will exceed the contract price, thereby reducing the contractor's assumption of contract cost risk.

(4) The third determination is that of the difficulty of the contractor's task. The contractor's task can be difficult or easy, regardless of the type of contract.

(5) Contractors are likely to assume greater cost risks only if contracting officers objectively analyze the risk incident to proposed contracts and are willing to compensate contractors for it. Generally, a cost-plus-fixed-fee contract would not justify a reward for risk in excess of 1 percent, nor would a firm fixed-price contract justify a reward of less than 5 percent. Where proper contract type selection has been made the reward for risk by contract type would usually fall into the following percentage ranges:

Type of contract	*Percentage ranges*
Cost-plus-fixed-fee	0 to 1
Cost-plus-incentive-fee including cost incentive only	1 to 2
Cost-plus-incentive-fee including cost, performance, and delivery incentives	1½ to 3
Fixed-price-incentive including cost incentive only	2 to 4
Fixed-price-incentive including cost, performance, and delivery incentives	3 to 5
Prospective price redetermination	4 to 5
Firm fixed-price	5 to 7

* * *

(d) *Record of contract performance.* (1) The purpose of this factor is to motivate contractors to improve their performance by rewarding them for excellent past performance and penalizing them for poor performance. Effective use of this factor requires that (i) reports on the various aspects of past performance be obtained and evaluated; and (ii) this information be used in such a way as to motivate contractors to improve their performance.

* * *

(6) The following factors are to be considered in evaluating a contractor's performance record:

(i) *Management.*

* * *

(ii) *Cost efficiency.*

* * *

(iii) *Reliability of cost estimates.*

* * *

(iv) *Cost reduction program accomplishments.*

* * *

(v) *Value engineering accomplishments.*

* * *

(vi) *Timely deliveries.*

* * *

(vii) *Quality of product.*

* * *

(viii) *Inventive and developmental contributions.*

* * *

(ix) *Small Business and Labor Surplus Area Participation.*

* * *

(e) *Selected factors.* The purpose of these factors, which may enter into a particular procurement situation, is to discourage reliance upon Government resources, and to encourage contractors to outstanding performance. Therefore, in assigning a composite profit percentage within the range of −2 to +2 for these Selected Factors, the Source of Resources factor will always be rated from 0 to −2 percent and the Special Achievement factor will always be rated from 0 to +2 percent. The Other factor may be rated with either a plus or a minus. These factors will rarely be of equal weight in a specific procurement. They should be assigned a weight as a group, in accordance with the following criteria:

(1) *Source of resources (Government or private).* Application of this factor calls for an

analysis of the contractor's dependence on Government financial assistance or material assistance in the form of facilities. Contractor reliance upon Government resources shall be discouraged by providing for less favorable profit consideration. Commercial facilities to be rented by the contractor will be evaluated as contractor furnished. Customary progress payments and guaranteed loans with normal guarantees (90 percent or less) shall not be weighted in this evaluation. However, other forms of financial assistance such as extraordinary progress payments, guaranteed loans with abnormal guarantees, or advanced payments shall be considered a minus factor. Similarly, the reliance on any other type of Government assistance, including facilities shall be evaluated as a minus from zero. The contractor who uses new Government resources for the performance of a contract will be penalized to a greater degree than the contractor who uses existing Government resources.

(2) *Special achievement, if any, required in the contract.* This factor indicates the need for extra profit consideration when outstanding performance is required. Such achievement may be in the form of a special technical requirement, such as production of some remarkable first, or achievements involving non-technical objectives, such as an extraordinarily fast delivery schedule.

(3) *Other.* Particular procurement situations may give rise to the desirability of using a profit factor other than those in subparagraphs (1) and (2) of this paragraph. Such factor shall be identi-

fied; and the reason for its use shall be documented in accordance with § 3.811.

[30 F.R. 5982, Apr. 29, 1965, as amended at 30 F.R. 14086, Nov. 9, 1965]

"§ 3.808—6 *Special profit consideration.*

"Contractors who develop military items without Government assistance are entitled to special profit consideration on those items. This consideration shall be in addition to the profit objective arrived at through the weighted guidelines method. One to four percent of recognized cost is established as the normal range of value for this profit factor. The criteria for selection of the specific percentage shall be the importance of the development in furthering defense purposes, the demonstrable initiative in determining the need and application of the development, the extent of the contractor's cost risk, and whether the development cost was recovered directly or indirectly from Government sources."

[30 F.R. 5985, Apr. 29, 1965]

Supreme Court, U. S.
FILED
JUN 26 1975
MICHAEL RODAK, JR., CLERK

74-1610

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-

BETHLEHEM STEEL CORPORATION,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

APPENDIX TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

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June 26, 1975

APPENDIX

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BETHLEHEM STEEL CORPORATION

v.

UNITED STATES

No. 44-68.

United States Court of Claims

March 20, 1970.

Albert R. Connelly, New York City, for plaintiff, James C. Hansen, New York City, of counsel.

James F. Merow, Washington, D.C., with whom was Asst. Atty. Gen. William D. Ruckelshaus, for defendant.

Before COWEN, Chief Judge, and LARAMORE, DURFEE, DAVIS, COLLINS, SKELTON and NICHOLS, Judges.

ON PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT AND DEFENDANT'S CROSS-MOTION FOR SUMMARY JUDGMENT

NICHOLS, Judge:

This is an action to recover amounts claimed to be due the plaintiff under labor and material escalation clauses in Contracts Nobs-3556 and Nobs-3648, under which plaintiff built five destroyers for the United States Navy at the shipyard it then owned at Quincy, Massachusetts. The contracting officer denied all escalation but in disputes clause appeals the Armed Services Board of Contract Appeals (ASBCA) allowed upward adjustments under the two contracts in the amounts of $1,064,151 and $876,028, respectively, which it computed as an allowance of 5% profit on costs after restoring certain cost disallowances the contracting officer had made, not here in issue. This being less than plaintiff's claims, it seeks review here under Wunderlich Act standards, 41 U.S.C. §§ 321 and 322. The parties have filed cross motions for summary judgment. We deny both motions and suspend further proceedings in this court to enable the parties to apply to the ASBCA for further findings of fact, pursuant to the opinion that follows.

The contracts were awarded by negotiation and included standard provisions requiring the contractor to exclude from its cost estimates all contingency allowances for increases in labor and material costs from the levels then obtaining, but on the other hand, allowing price increases according to an agreed formula reflecting labor and material cost increases experienced in the contract period by shipbuilders agreed upon as representative. There is no dispute that such cost increases did occur, nor as to the contract price increases that would result, except for Article 6(e),

which reads as follows:

> (e) The Contracting Officer may deny, in whole or in part, any upward adjustment in the contract price required under this Article if the Contracting Officer finds that such adjustment is not required, in whole or in part, to enable the Contractor to earn a fair and reasonable profit under this contract.

This contract language came before us for interpretation three years ago in Newport News Shipbuilding & Dry Dock Co. v. United States, 179 Ct.Cl. 97, 374 F.2d 516 (1967). The nub of the controversy here is how to apply the rulings then made to the somewhat different facts and regulation before us now. These facts are stipulated, so far as they go, the Board having taken no testimony. The refusal of any escalation clause increases by the contracting officer, and the refusal of portions of the amounts otherwise accrued, by the ASBCA, resulted from their beliefs that the amounts they denied were not required to enable plaintiff to earn fair and reasonable profits under the contracts. Both decisions were, however, rendered before ours in Newport News. Plaintiff would remand for further Board proceedings in light of Newport News, but defendant says Newport News is not applicable and the Board decision is entitled to finality.

The Navy decided to build three destroyers (DD 936-938) in a private yard. On or before January 25, 1954, it received proposals for major east coast concerns as follows, per ship:

Bath Iron Works	$15,492,000
Newport News	16,800,000
Quincy (plaintiff)	18,674,000
New York Ship	19,234,000

As usual in negotiated procurement, all submitted cost estimates which showed that they anticipated profits of 9.3% of cost, in the case of one, to 9.4% for another, and 10% in the cases of Quincy and the fourth. Defendant, however, desired to award the vessels to Quincy because Quincy was about to run out of work and if it did, management would probably close down the yard, which was one of the largest and best equipped in the world. Moreover, plaintiff maintained at Quincy the design and engineering staff for all its several other shipbuilding and repair yards on both coasts. The anticipated closure, therefore, would have effected a material reduction in the capacity of the shipbuilding industry to produce for national defense in case of any emergency. Since World War II, the Navy had on one or more occasions bailed all of the above named companies out of potentially disastrous slumps in their business by awarding them shipbuilding contracts when they were not the lowest bidders. They were painfully dependent on the Navy, for all other customers together accounted for but 35% of their business, yet even the Navy's orders were at a modest level pending the wearing out or obsoletion of the vast tonnages delivered in World War II. All four yards were, therefore, operating at a minor fraction of capacity. The three other than Quincy, did have enough orders to keep them busy at the then level of activity for a year or two to come, so it was only Quincy that was in immediate danger

of shutdown. The Navy, accordingly, decided to negotiate with Quincy.

To avoid making a bad situation worse, the Navy asked plaintiff to reduce its bid and it took $1,000,000 off the price of each ship, and the award was made at $17,674,000 per unit, which was still considerably over the bids of Bath Iron Works and Newport News. The revised cost estimates remained unchanged, but showed that plaintiff was now estimating a profit of $698,000 instead of $1,698,000. There was, however, no contract provision that plaintiff's profit would be any particular figure.

One asks next why plaintiff estimated its costs so much above competitors who were, by its account, no more efficient, and had no better plant. The answer is that the three destroyers would have utilized only 5% of Quincy's capacity. In estimating its costs, Quincy calculated it would have no other business and the contract for the destroyers would have had to carry the overhead of that vast establishment. Evidently the Navy had to contribute towards this overhead if it was to persuade plaintiff not to close the plant down. Bath, being smaller and busier, was far more favorably situated with respect to overhead. We conclude that in the events that materialized, that is, Quincy's receiving other orders, the allocable overhead would have been less, and therefore the costs.

The circumstances of this award are given because, as will appear, they afford the basis for defendant's argument that Newport News is not applicable as a precedent. The facts stated above were either

FEED THROUGH

found by the Board, or else appear as testified in the printed transcript of a hearing conducted by a subcommittee of the House Armed Services Committee in February and March, 1954, to inquire into the award of Nobs-3556 and the rejection of the low bids. The parties here attached it to their stipulation as Exhibit 6, without restriction as to relevance or use, so we use it as uncontradicted evidence.

The other contract in this litigation, Nobs-3648, was awarded plaintiff later the same year and called for construction of two additional destroyers, DD 943 and 944, at a negotiated price of $16,250,000 per ship, including an estimated profit of $698,000. There was, therefore, a cost saving estimated. It had the same limited escalation as Nobs-3556. There were other awards not involved in this litigation while the five destroyers were under construction, notably a nuclear powered cruiser and three guided missile frigates. Plaintiff delivered the first destroyer on November 30, 1956, three more in 1957, and the last on February 26, 1958. There were, as usual, change orders and equitable adjustments therefor, not now in dispute. The costs, except for those extras and escalatable labor and material, were lower than estimated, plaintiff says due to cost savings all along the line.

The financial results under the two contracts are set forth in detail in the Board findings and need not be repeated here at this time, especially since the case may come before us again. To pose the legal problem it suffices to say that labor and material escalation before any

Article 6(e) exclusion, totalled $3,347,500 and $2,404,900 under the two contracts, respectively. The profit before any escalation, but reflecting the Board's decision as to allowable costs, would be $1,597,000 under Nobs-3556 and $775,000 under Nobs-3648, making 3% and 2.3% of cost respectively. The profit with partial escalation allowed by the Board as stated above would be 5% of cost under both contracts. The profit with full escalation would be $4,990,000 under Nobs-3556 and $3,180,000 under Nobs-3648, being 9.3% and 9.6% of cost respectively. That the profit with full escalation is so much over the contract estimate is due, as said above, to savings in non-escalatable costs, but the Board did not perform any analysis to determine how these savings were accomplished. The Board also considered profits as a percentage of price, but we need not go into that here.

Our Newport News decision interprets the Article 6(e) language together with a Department of Defense regulation in effect when the administrative decision was made, 22 F.R. 5927, 32 C.F.R. §§ 3.808 and ff. The former we viewed as requiring an administrative determination as to what a fair and reasonable profit would be under the contract incorporating the clause in light of the performance history and financial results. Such a determination would be a finding of fact, final in this court if supported by substantial evidence and made in accordance with law. The latter, the regulation, we found to contain language telling how such a determination was to be made, whether related to initial pricing or any sort of contract repricing. There was nothing to

FED THROUGH

show that in making the findings there involved, the Board had employed or intended to employ the technique the regulation prescribed, and several statements in the Board opinion afforded indications that the regulation was not deemed applicable. We suspend further action to allow the parties to apply for further Board findings, without intimating any opinion, or indeed, having one, whether the level of fair and reasonable profits as the Board had determined was adequate or not.

That case has stood on the books for three years now without any sort of challenge on defendant's part, not even a motion for reconsideration. Since our holdings deviated to some extent from those urged upon us by either party, they may well have come as somewhat of a surprise, and a motion for rehearing on the ground of surprise would not have lacked dignity. As things are, this is the first chance we have had to learn defendant's views. Defendant apparently agrees with us to a large extent, and appears in general willing for Newport News to be followed in cases that reproduce its facts. That carries important implication.

The contracts here, as in Newport News, were made before the Pentagon had on the books any regulation prescribing, except in redeterminations, any technique of determining a level of reasonable profits for a defense contractor. The involved regulations, however, when made, appeared to be remedial, meant to safeguard defense contractors against determinations as to a reasonable profit level, arbitrary, perhaps biased, or founded on "seal-of-the-pants intuition", which contracting officers might

make without proper guidelines. There is no reason to postulate an intent to withhold such safeguards from parties to then existing contracts, nothing to that effect appearing either in the contracts or the regulation. Defendant refers, properly we think, to Thorpe v. Housing Authority, 393 U.S. 268, 89 S.Ct. 518, 21 L.Ed.2d 474 (1969), as being in agreement with our position. Since Government officials are presumed to act properly, it is reasonable to suppose that the Pentagon would not have promulgated clauses such as Article 6(e) unless contracting officers could employ established techniques and guidelines, even if unpublished and therefore would not act arbitrarily. If any contractor supposed he had rights vested under a contract which were substantially subverted by a regulation later adopted as to how to determine reasonable levels of profits, he might come into court and show it. See Thorpe, supra, at p. 283, 89 S.Ct. 518. In the absence of such a showing we cannot assume it would occur.

Defendant passes over in silence the fact noticed by the dissenting judges in Newport News, that plaintiff there had done nothing to alert the Board to the fact it was not following the Department of Defense's regulations. That is equally true of the instant case. It is indeed, generally, a salutary rule that a party cannot assign an error here that he has not given the administrative tribunal a chance to correct. But the points plaintiff did make below were of a nature that should have alerted the Board to test what it was doing against applicable regulations. We think an exception in such a case must be made in the interests

of fairness when the error consists of a mutual ignoring of a whole body of applicable agency regulations. Agency officials have considerable practical power to steer the choice of issues to ground of their selection, in proceedings before their agencies. If attention is totally diverted from applicable regulations the responsibility for this error is not equal. Agency officials have the means and the duty to be aware of their own regulations to a greater extent than outsiders. It is not fair to throw the consequences of such a mutual mistake wholly on the party least responsible for causing it. We say this not meaning to impugn the good faith of the Pentagon officials, who apparently quite sincerely believed that a clause such as Article 6(e) was somehow something other than the kind of pricing and repricing power the guidelines were meant to cover. The arguments made to us by both sides in Newport News reflected a state of great confusion on both sides as to what Article 6(e) was meant to do. The requirement for exhaustion of administrative remedies is not inflexible in some exceptional circumstances. E.g., Mallow v. United States, 161 Ct.Cl. 207, 212 (1963).

This brings us at length to the difference which defendant says exists between this case and Newport News. It is not that the regulations involved are new, though they are, as set forth below. Defendant says that this case falls clean outside all published guidelines for determination of a reasonable level of profit, because the contracts were awarded to other than the low bidder for the purpose of continuing the existence of an essential defense facility. This position does not require defendant to take issue with our

holding in Newport News and it does not, yet it likewise does not require defendant to argue, as indeed it could not, that the Board here paid any attention to guidelines or techniques for determining a reasonable profit level, as published by the Department of Defense or anyone else, and in effect at the time the Board decided. No such publication is ever alluded to in the Board decision. It does indeed use guidelines, but they are "do-it-yourself" guidelines constructed by the Board itself out of arguments and suggestions of counsel. As already pointed out, counsel on neither side suggested to the Board that it should follow the published guidelines, and that is the obvious reason why it did not do so.

A Department of Defense regulation that was in effect at the time of the instant Board decision, and also that of the contracting officer, was published in 1963, 28 F.R. 12546, 12555, amending 32 C.F.R. Part 3, §§ §§ 3.808 and ff. It supersedes the one we construed in Newport News. It states and describes, with copious illustrations, the "Weighted guidelines method" of determining reasonable levels of contractor profits. Defendant does not now deny that it would govern most decisions limiting or refusing otherwise justified labor and material escalation under Article 6(e), and there is nothing in it that suggests an intent to narrow the former scope. But, defendant says, this case is an exception. However, the regulation itself in § 3.808-2(b), enumerates the recognized exceptions to it, and the situation here involved is not on the list. Any other exception must be authorized by the head of the procuring agency, and no such authorization is asserted here. On the other hand, the statute defendant says

authorized this type of procurement to keep a contractor in business. The Armed Services Procurement Act of 1947 § 2(c)(16), now revised and codified as 10 U.S.C. § 2304(a)(16) (1964), does not speak in terms of any exemption from profit guidelines ordinarily applicable.

If defendant's postulated exemption exists, it must be a large one. The record shows that all of plaintiff's above named competitors in the shipbuilding industry were awarded major contracts at one time or another between World War II and 1954, when they were not the low bidders, for reasons the same as those which animated the award of Nobs-3556 to plaintiff. The situation recurs so commonly in our litigation with other industries heavily dependent on defense work, that we may take judicial notice of it; a rigid adherence to procurement from the lowest bidder only is viewed in the Pentagon as gradually freezing out the competition and leading into single-source procurement. The subcommittee recognized the validity of this view in its hearing on the instant award, as did the whole Congress, of course, in enacting 10 U.S.C. § 2304(a)(16). It would be strange if so large an exception to the use of the "Weighted guidelines method" went unmentioned in the enumeration of exceptions in the regulation itself. The new regulation requires use of the guidelines if cost analysis is required. § 3.808-1(b). Cost analysis is required with respect to negotiated fixed price contracts with escalation, all of which these are. § 3.807-3(a)(2). To put it succinctly, the alleged exception has every earmark of having originated in the active mind of defense counsel herein, not in the perhaps more rigid thinking of the Pentagon.

Defendant says that plaintiff agreed to accept a profit of around 5% in consideration of being awarded the contract, though not the low bidder, and therefore use of the "Weighted guidelines method" to produce a higher profit would be so unfair that an exception to the method must be implied. The contracts, however, reflect that plaintiff agreed only upon a price. The alleged agreement upon a profit came in the revised cost estimates, which showed estimated costs only $698,000 per unit below the agreed price. Both parties must have been aware that this estimated cost was a figure plucked from the atmosphere. Mr. Strohmeier, plaintiff's vice president, testified at the Congressional hearing, without contradiction, that the entire excess of his company's cost estimates over Bath's was due to the higher allocation of overhead, and this difference, in turn, resulted from the hypothesis, that the Quincy yard would be operating at but 5% of capacity, having no other work than the three destroyers. Even so, on that hypothesis, the estimated allocation he thought was insufficient. If his company built the three destroyers and had no other construction at the Quincy yard, he expected it to suffer a loss. On the other hand, if it received enough other business so it could operate at a "normal" level, its contract costs would fall to approximately Bath's estimates. In that event, which was surely always possible, and wholly apart from any savings due to efficient manufacture, there would have been a large windfall profit under Nobs-3556, for whose recapture the contract made no provision if one disregards the statutory renegotiation article. Defendant does not and could not regard that

article as contributing in any way to its argument that plaintiff agreed to a profit level of exactly 5%. The alleged agreement to a 5% level, in a contract that viewed prospectively could have resulted in anything from a loss to a windfall profit level, according to its terms, must be regarded as located in defendant's counsel's eyes alone.

As already noted, plaintiff in preparing its cost estimates was required to assume there would be no increases in labor and material costs, and in analyzing the possibilities of profit in the contract, we have up to this point done so likewise. In the more probable event there were such increases, the escalation clause became operative and in general its effect would be, absent Article 6(e), to stabilize the profit or loss at a fixed dollar (not percentage) figure against any degree of labor and material cost inflation. There might be some small profit or loss resulting from the escalation clause itself, as the plaintiff's own experienced labor and material costs might be more or less than the general industry experience used to fix the escalation indices. There was nothing in the escalation clause before Article 6(e), agreeing to a 5% profit. In article 6(e) there was certainly a possibility that the profit would be cut, but 5% is not mentioned.

We have now examined every pertinent part of the contract and nowhere find agreement to a 5% profit level, while we do find provisions that enable a profit much exceeding 5%, whether or not escalation was required, depending on conditions which were perfectly foreseeable

and which plaintiff would certainly exert itself to bring about, i.e., a normal utilization of the yard. On the other hand, the $698,000 profit estimate contemplated a state of inadequate utilization which could hardly have been expected or allowed to be other than temporary.

While we say plaintiff did not agree to 5%, we do consider that a high bidder given a contract award purely to keep him in business, might expect this fact to be considered as unfavorable to him under any rational system of profit limitation. Defendant's view that the "Weighted guidelines method" would fail to give weight to this apparently is basic to its argument that the method is so unsuited to the instant procurement that the exception of it from the regulation must be implied. We do not read the regulation that way. The plaintiff's overhead allocated to Contract Nobs-3556, was by the evidence in the record entirely out of line with that which the lower bidders would have allocated. A Board applying the method would be required by § 3.808-5(b)(3) to analyze the overhead items of cost and determine "how much they contribute to contract performance." A range of 4-7% is assigned to "manufacturing overhead" and a range of 6-8% to general and administrative expenses. We think the Board would be within its charter in denying a return on that part of the overhead which exceeded the allocation of other shipbuilders. Moreover, under § 3.808-5 (e)(1) the Board is to make an analysis "of the contractor's dependence on Government financial assistance * * *." If the dependence is great, it is a minus factor in determining the allowable profit.

While the point may be debatable, we think that the addition of a bonus to a contract price to enable the contractor to maintain uneconomically large facilities in being is in reality a form of Government financial assistance and should be treated as such.

On the other hand, the guidelines attach favorable consideration in § 3.808-5(e) to "Contractor's assumption of contract cost risk." The guidelines here look with least favor on a cost plus fixed fee contract with full cost reimbursement, and most favorably, at the other end of the scale, on a "closely priced firm fixed-price contract" for a complex item, which "would reflect a complete assumption of cost responsibility." We have here a firm fixed price contract for a complex item, with only limited escalation, and according to Mr. Strohmeier, a real possibility of loss prospectively considered, if other business was not obtained. It would appear Contract Nobs-3556 at least is, on this factor, closer to the favorable than the unfavorable end of the scale. (Of course, we do not know from the record to what extent the loss would have been an actual cash drain and to what extent a paper write-off.) The guidelines appear to be the Pentagon's best thinking on the subject of the proper administration of profit limitation clauses, and this favorable consideration of close pricing and assumption of risk stands in stark contrast to the Board's unfavorable consideration of what is apparently the same thing: plaintiff's willingness to accept a price shaved close above the estimated cost.

It would, of course, be improper

for us to make a determination ourselves under the "Weighted guidelines method" for the reasons explained in Newport News and for the further reason that the record is inadequate. To use the method one needs to be well informed. The Board will no doubt supplement the stipulation with further evidence. We do not know whether, by proper application of the method, plaintiff will fare better or worse than 5%. Plaintiff desires to take its chances under the "Weighted guidelines method" and it has a legal right to do so.

As we have said, we see no injustice or anomaly in applying profit limitation techniques, as the Pentagon may have amended and prescribed them from time to time, up to the date of the determination. We would presume that changes were intended to clarify and simplify, as well as to reduce the impact of subjective factors in the mind of the administering official. To some extent amendments may reflect earlier departures in actual practice, to a large extent no doubt they are the product of experience. If anything has been slipped in which would impair vested rights unless limited to prospective application only, let it be pointed out. If we have erred in thinking the "Weighted guidelines method" is feasible to apply to the instant contracts, the Pentagon even now could amend or supplement its regulation, and the Board would be bound, provided no impairment of vested rights was attempted. Any amendment purporting to reaffirm the position now claimed, that officials determining a reasonable level of profit under clauses such as Article 6(e) are not subject to any published guidelines

whatever in certain cases, at least would advisedly be made in light of the recent statement of the Supreme Court: "* * * a broad, roving authority, a type of administrative absolutism [is] not congenial to our law-making traditions." Gutknecht v. United States, 396 U.S. 295, 90 C.Ct. 506, 24 L.Ed.2d 532.

CONCLUSION

Plaintiff's motion for summary judgment and defendant's cross motion for summary judgment are denied. Further proceedings are stayed pursuant to Rule 167 for a period of six months to enable the parties to obtain further fact findings in accordance with this opinion under the applicable guidelines in published regulations. Plaintiff shall advise the commissioner of the status of the case before the Armed Services Board of Contract Appeals at intervals of not less than 60 days beginning with the date of this order, as prescribed in Rule 167(e) and (f).

DAVIS, Judge (concurring):

Newport News, which I consider now binding on me, settled the issue of whether the ASPR guidelines were required to be followed even though neither party invoked them before the Board. That being so, I agree with the court, for the reasons it gives, that those regulations apply in this case as well, and on that basis I join in the disposition requiring them to be applied here.

SKELTON, Judge (dissenting):

I respectfully dissent. In my opinion,

Newport News Shipbuilding & Dry Dock Co. v. United States, 179 Ct.Cl. 97, 374 F.2d 516 (1967), does not control this case and it should not be sent back to the board (ASBCA) in order to allow it to use the guidelines of the Department of Defense regulation published in 1963 (28 Fed. Reg. 12546, 12555, amending 32 C.F.R. §§ 3.808 and ff. (part 3)), to determine the profit of the plaintiff in this case, for the following reasons:

(1) This regulation was not in existence at the time the contracts involved here were executed and could not have been contemplated by the parties. Although the same situation existed in Newport News, the facts in the two cases are completely different. There the court held that the regulation must be applied to the original competitive prices as well as to escalated prices, but that cannot be done in the instant case because the bids here were not competitive. It is improper to apply the regulation retroactively under these circumstances in our case. In fact, it is impossible to apply the decision in Newport News to the original prices here.

(2) The contracts before us were negotiated between the parties and were not the result of competitive bids. In fact, they amounted to a subsidy by the government, and without them the plaintiff would have had to have closed its doors and gone out of business. Plaintiff was not the lowest bidder, as two other companies submitted lower bids. The government gave it the contracts after negotiation to keep it in operation. As a result, the plaintiff has

been subsidized to the extent of a five percent profit on the undertaking, but instead of being grateful for this generosity, now sues for more. It is impractical, if not impossible, to apply the regulation to the prices thus negotiated between the parties.

(3) The parties submitted guidelines to the Board that they wished it to consider. The Board did consider them fully, as indicated in its opinion. The plaintiff did not ask the Board to consider any additional guidelines and did not mention those set forth in the regulation which was in force at the time of the Board's decision. No request was made that the guidelines in the regulation be considered. It is too late, in my opinion, for the plaintiff to make such a request, and it is error for us to allow it to do so.

(4) The Board found as a fact that the parties agreed that plaintiff's profit would be five percent, and plaintiff has not challenged this finding. Consequently, the finding is final and we are bound by it and have no authority to set it aside.

I would grant defendant's cross-motion for summary judgment, deny plaintiff's motion, and dismiss plaintiff's petition.

ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeals of --	)
	) ASBCA Nos.
Bethlehem Steel Corporation	) 10316 and
	) 10317
Under Contract Nos. NObs-3556 and NObs-3648)	(Reinstated)

APPEARANCES FOR THE GOVERNMENT:
Samuel Pinn, Jr., Esq.
Counsel, Naval Ship Systems Command
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Associate Counsel

APPEARANCES FOR THE APPELLANT:
E. J. O'Brien, Esq.
Bethlehem Steel Corporation
Bethlehem, Pennsylvania

DECISION ON GOVERNMENT'S MOTION FOR AN ORDER ESTABLISHING THAT THE ASPR NON-WEIGHTED PROFIT GUIDELINES ARE APPLICABLE TO DETERMINING CONTRACT PRICE

STATEMENT OF FACTS

These appeals are here on remand from the Court of Claims pursuant to the order of the Court in Bethlehem Steel Corporation v. United States, Ct. Cl. No. 44-68 (Decided March 20, 1970). The appeals were previously decided by this Board in an opinion dated 16 June 1966 reported in 66-1 BCA par. 5639.

The facts giving rise to this dispute will not be repeated here since they are set forth in the earlier Board

decision and in the opinion of the Court of Claims. As the Board stated previously, "The crucial proviso about which the dispute arose is Article 6 of both contracts entitled Price Adjustments and commonly referred to as an escalation clause, which in pertinent part reads:

> '(e) The Contracting Officer may deny, in whole or in part, any upward adjustment in the contract price required under this Article if the Contracting Officer finds that such adjustment is not required, in whole or in part, to enable the Contractor to earn a fair and reasonable profit under this contract'."

The two contracts called for a total of five destroyers. After they had been performed appellant made a claim for price escalation pursuant to Article 6 which was denied by the contracting officer as not required to enable appellant to earn a fair and reasonable profit under either contract. In deciding the appeals subsequently taken from the final decisions of the contracting officer, this Board sustained appellant's position in part, and allowed escalation to the extent that appellant would realize a 5% profit on costs. Appellant had claimed escalation sufficient to enable it to earn a profit of 9.3% on Contract NObs-3556 and 9.6% on NObs-3648.

Appellant then filed suit in the Court of Claims endeavoring to recover a greater amount of escalation than had been allowed by the Board. The Court

reached a result similar to its decision in Newport News Shipbuilding and Dry Dock Company v. The United States, 179 Ct. Cl. 97 (1967), i.e., that the Board had erred in not determining fair and reasonable profit in accordance with what the Court regarded as the applicable guidelines for establishing profit objectives set forth in the Armed Services Procurement Regulations (ASPR) at the time the Board rendered its decision. For the purpose of determining the Bethlehem appeals, the Court said that the Board should have applied the so-called "weighted guidelines" as set forth in ASPR Part 3-803, effective 15 August 1963. In its Newport News opinion the Court said that the Board, in deciding the Newport News appeals should have applied the so-called "non-weighted guidelines" set forth in ASPR 3-808 effective January 1960. The Board had decided the Newport News appeals in 1962. The "non-weighted guidelines" were superseded by the "weighted guidelines" in 1963. The "weighted guidelines" appear in the presently effective ASPR 3-808.

In reaching its decision in the Bethlehem case, the Court discussed the type of analysis which it thought the Board might undertake in applying the "weighted guidelines" to determine fair and reasonable profit on the basis of relevant facts. However, the Court did not purport to determine the amount of profit to which appellant might be entitled through application of the weighted guidelines. In the language most relevant to resolving the interlocutory question now before us, the

Court said:

> "It would, of course, be improper for us to make a determination ourselves under the 'Weighted guidelines method' for the reasons explained in Newport News and for further reason that the record is inadequate. To use the method one needs to be well informed. The Board will no doubt supplement the stipulation with further evidence. We do not know whether, by proper application of the method, plaintiff will fare better or worse than 5%. Plaintiff desires to take its chances under the "Weighted guidelines method' and it has a legal right to do so.
>
> "As we have said, we see no injustice or anomaly in applying profit limitation techniques, as the Pentagon may have amended and prescribed them from time to time, up to the date of the determination. We would presume that changes were intended to clarify and simplify, as well as to reduce the impact of subjective factors in the mind of the administering official. To some extent amendments may reflect earlier departures in actual practice, to a large extent no doubt they are the product of experience. If anything has been slipped in which would impair vested rights unless limited to prospective application only, let it be pointed out. If we have erred in thinking the 'Weighted guidelines method' is feasible to apply to the instant

contracts, the Pentagon even now could amend or supplement its regulation, and the Board would be bound, provided no impairment of vested rights was attempted. Any amendment purporting to reaffirm the position now claimed, that officials determining a reasonable level of profit under clauses such as Article 6(e) are not subject to any published guidelines whatever in certain cases, at least, would advisedly be made in light of the recent statement of the Supreme Court: '* * * a broad, roving authority, a type of administrative absolution [is] not congenial to our law-making traditions.' Gutknecht v. United States 396 U.S. 295, (decided January 19, 1970), slip op. at p. 10.

CONCLUSION

"Plaintiff's motion for summary judgment and defendant's cross motion for summary judgment are denied. Further proceedings are stayed pursuant to Rule 167 for a period of six months to enable the parties to obtain further fact findings in accordance with this opinion under the applicable guidelines in published regulations. Plaintifff shall advise the commissioner of the status of the case before the Armed Services Board of Contract Appeals at intervals of not less than 60 days beginning with the date of this order, as prescribed in Rule 167(e) and (f)."

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After the Court's decision was issued, the Navy applied to the ASPR Committee for a "deviation" providing for the inapplicability of the weighted guidelines to ship construction contracts executed prior to 1963 which contain the profit limitation feature of the escalation clause (Article 6(e)). Eleven such contracts were listed, including the two involved in these appeals. In his memorandum to the Chairman of the ASPR Committee dated 22 May 1970, the Navy Legal Member of the Committee discussed the Court of Claims and Board decisions in Newport News and Bethlehem, quoted portions of the Court's Bethlehem decision, and advanced reasons for the Navy's position that "the weighted guidelines were not intended to be retroactive so as to affect contracts executed prior to the promulgation of the Revision of August 1963."

The ASPR Committee met on 3 June 1970 to consider Case No. 70-2-16 referred to in the minutes of the meeting as "Deviation from ASPR 3-808, Profit Guidelines." After considering the memorandum submitted by the Navy Legal Member, the Committee reached the following decision as recorded in the minutes:

> "The Committee agreed that mandatory application of the weighted guidelines retroactively to contracts entered into before adoption of such guidelines, particularly with respect to contracts containing the . . . escalation clause, was not intended and a deviation is not required. The

> Committee also agreed that application of the weighted guidelines to pre-existing contracts is not appropriate, and on a consensus basis that it is not feasible, since they effected a substantive change in the standards existing at the time the contracts were entered into and were intended for the development of a profit objective for negotiation of future contracts. . . ."

The Committee referred, in this connection, to "Notes and Filing Instructions" for promulgation of the weighted guidelines, which set forth the general policy reasons for the issuance of these guidelines, and prescribe mandatory use of them to all "applicable procurements" initiated after 1 January 1964.

In the final two paragraphs of the minutes it is stated that:

> "Notwithstanding the foregoing, the Committee agreed that to the extent that others may consider the application of the weighted guidelines to be mandatory in such circumstances, a deviation is approved.
>
> "In taking this action the Committee recognized that this would leave for consideration, as applicable to the listed contracts, the ASPR 3-808 non-weighted guidelines which preceded adoption of the weighted guidelines. The former were not regarded as effecting any significant substantive change."

The Executive Secretary of the ASPR

Committee has certified that the nine Committee members present and voting agreed unanimously on the above actions.

Under letter to the Board dated 26 June 1970, the Government filed a motion seeking rulings by the Board:

"a. That the minutes of the ASPR Committee meeting of 3 June 1970, re Case No. 70-2-16, be admitted in evidence.

"b. That by virtue of said action of the ASPR Committee, the Board enter an appropriate order determining that the procedural non-weighted guidelines of ASPR 3-808, rather than the weighted guidelines, in the regulation which will be applied by the Board to determine whether or the extent to which, an upward adjustment in the contract price under the escalation clause of the subject contracts is required to enable the contractor to earn a fair and reasonable profit under the contracts."

Appellant opposed the motion and transcribed oral argument was presented by both sides at a prehearing conference held on 9 September 1970. Briefs on issues raised by the motion were filed by both parties and exchanged on 19 October 1970. Reply briefs were exchanged on 19 November 1970.

DECISION

The Court of Claims has remanded this case to the Board in order that the parties may "obtain further fact findings," in accordance with the Court's opinion "under the applicable guidelines in published regulations." The issue raised by the Government's motion is the narrow one of whether we are required by the Court's decision to make those "fact findings" through application of the ASPR weighted guidelines, or whether we are required by that decision to apply the non-weighted guidelines as proposed by the Government. The issue does not involve an exercise of discretion by the Board as to which guidelines to apply, but rather involves a determination of what the Court has ordered it to do.

Had the Court not said what appears in the penultimate paragraph of its opinion, which is the second of the three paragraphs quoted in full above, we would have no doubt that the Court has required us to determine fair and reasonable profit through application of the weighted guidelines to the facts as stipulated or found in a further proceeding on the merits. Indeed the Court said in the first paragraph quoted in full above that "Plaintiff desires to take its chances under the 'weighted guidelines method' and it has a legal right to do so." However, the Court immediately thereafter said that:

> ". . . we see no injustice or anomaly in applying profit

> limitation techniques, as the Pentagon may have amended and prescribed them from time to time, up to the date of the determination . . . If we have erred in thinking the 'Weighted guidelines method' is feasible to apply to the instant contracts, the Pentagon even now could amend or supplement its regulation, and the Board would be bound, provided no impairment of vested rights was attempted."

Appellant would have us ignore the language just quoted as inconsequential dicta. However, the Court's order contained in the final paragraph of its opinion does not refer specifically to the weighted guidelines, but instructs the Board to make findings "in accordance with its opinion under the applicable guidelines in published regulations." The penultimate paragraph of the Court's opinion is a part of the opinion in which the Court has stated that the Board under certain conditions would be required to apply guidelines other than those now set forth in ASPR 3-808. We accordingly are obliged to accord that paragraph the legal effect which it merits.

Appellant does not contend that the non-weighted guidelines are not "published guidelines" in the sense meant by the Court. However, appellant contends that the Board should not consider itself "bound" to give effect to the actions of the ASPR Committee on the ground that those actions did not amount to an "amendment" or "supplement" to the weighted guidelines by the "Pentagon." Appellant further contends that even if the ASPR

Committee's actions do amount to such an amendment or supplement, the application of the non-weighted guidelines to the "instant contracts" would deprive appellant of a "vested right."

In using the term "Pentagon" we think that the Court was referring to those Department of Defense officials authorized to establish or modify provisions of the Armed Services Procurement Regulations. DOD Instruction No. 5126.3 dated 20 December 1961, which prescribes the composition, functions and authority of the ASPR Committee provides, in Paragraph 825.50 that:

> "A. With respect to matters, other than major policy matters, as to which the members are in accord, action of the Committee shall be considered as having the final approval of the Military Departments and the Defence Supply Agency without further review by them . . . ."

Similarly, ASPR 1-109.3, applicable to "Deviations Affecting More than One Contract or Contractor" provides in part that:

> ". . . deviations from this Regulation or a Department of Defense Directive will not be effected unless approved in advance by the Assistant Secretary of Defense (Installations and Logistics); provided, however, that unanimous approval by the members of the ASPR Committee will constitute approval of the Assistant

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> Secretary of Defence (Installations and Logistics) of all matters except those involving major policy . . . ."

In ASPR 1-109.1, one type of deviation is described as follows:

> "(vii) when a policy, procedure, method or practice of conducting procurement actions of any kind at any stage of the procurement process is covered by ASPR, any policy, procedure, method or practice which is inconsistent with that set forth constitutes a deviation; . . ."

Moreover, ASPR 3-808.2(b) provides for exceptions to applicability of the weighted guidelines. Although ship construction contracts containing the escalation clause are not listed among the specific exceptions in subparagraph (b)(1), subparagraph (b)(2) provides that:

> "Other exceptions may also be made in the negotiation of contracts presenting unusual pricing situations when specifically authorized by the Head of a Procuring Activity. Such exceptions shall be justified in writing and authorized only in situations where the weighted guidelines method is determined to be unsuitable."

We think that the ASPR Committee possessed ample authority, pursuant to the above regulatory provisions, to determine on behalf of "the Pentagon," that the weighted guidelines are not

"feasible" for application to a retroactive determination of fair and reasonable profit as required by the escalation clause, and that the non-weighted guidelines should be so applied in lieu thereof. Appellant has suggested that such determinations are matters of "major policy" and that the ASPR Committee was not empowered to take final action thereon. However, we are not aware of any established criteria for determining what is or is not "major policy" for the purposes of ASPR Committee action. Such determinations are within the purview of policy making officials of the Department of Defense, not this Board.

Appellant has also challenged the propriety of the ASPR Committee actions on the basis of what appellant regards as procedural irregularities. Appellant points to the ex parte nature of the proceeding, a feeling on the part of the appellant that the Committee members lacked sufficient information to arrive at a considered decision, and the speed with which the action was taken. However, we are not aware of any provision of law that prohibits ASPR Committee action on matters brought to its attention ex parte by a procuring agency. The adequacy of the information presented to the Committee, and the speed with which it reached its decision are matters within the discretion of the Committee.

Appellant has endeavored to demonstrate to the Board that the weighted guidelines are in fact feasible to apply to the "instant contracts." In a proper case we might so determine. Norair

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Engineering Corporation, ASBCA No. 10856, 67-2 BCA par. 6619. However, the Court of Claims has left such a determination to "the Pentagon" as distinguished from the Board. We are obliged to observe this distinction in the absence of evidence that the ASPR Committee has acted arbitrarily in making its determinations. In this regard, appellant apparently contends that the ASPR Committee ignored a definition of "feasible" as including what is "possible" or "practicable" or "capable of being done." However, the same dictionary also defines the word "feasible" as including what is "suitable" or "reasonable." (Webster's New International Dictionary, Second Ed., p. 926.) It is clear that the ASPR Committee had the latter meaning in mind when it determined that the weighted guidelines were not feasible "since they . . . were intended for the development of a profit objective for negotiation of future contracts." Even if it were indeed "possible" or "practicable" to apply the weighted guidelines, we do not regard the Court as having used "feasible" in the narrow sense proposed by appellant. And we do not regard the grounds cited by the ASPR Committee for its actions as unreasonable.

Appellant has further contended that the action of the ASPR Committee is an attempt to overrule the decision of the Court. In making this contention, appellant assumes that the Court has determined that the Board is obligated to apply the weighted guidelines as distinguished from any other guidelines for the purpose of determining the profit to which appellant is entitled.

As indicated above, we do not read the Court's opinion in that manner. The Court was essentially determining how, in its opinion, the Board erred in arriving at its initial result. In effect the Court was telling the Board that it must apply the weighted guidelines unless "the Pentagon" were to determine that the weighted guidelines are not feasible and appropriately amends or supplements its regulations without depriving appellant of "vested rights." If "the Pentagon" were to acomplish such actions, the Board would be "bound" to apply the amended or supplemented regulations. It might be contended that the ASPR Committee went beyond an "amendment" or "supplement" when it determined that the non-weighted guidelines should be made applicable to determining profit under contracts of the kind involved here. However, from a reading of the last sentence of the penultimate paragraph of the Court's opinion, it is apparent that the Court was not particularly concerned with how one might characterize the action taken by "the Pentagon," but was insistent upon the applicability of "published guidelines" to the resolution of this controversy. From its consideration of the Newport News case, the Court was well aware of the non-weighted guidelines. And in its motion for summary judgment, the plaintiff (Bethlehem) further called the Court's attention to the non-weighted guidelines as well as to the weighted guidelines. In this connection it is noteworthy that in none of the papers which it filed with the Court did Bethlehem specifically ask the Court to order application of the weighted guidelines, as distin-

tinguished from any other guidelines which Department of Defense officials might regard as more suitable.

Appellant's final principal contention is that if we give effect to the action of the ASPR Committee we would be depriving appellant of a vested right, a consequence not permitted by the Court. Appellant is saying in effect that it has a vested right to application of the weighted guidelines. Both parties have cited a variety of cases which bear on the question of what might be characterized as a "vested" right in circumstances not analogous to the present controversy, e.g., Greene v. United States, 376 U.S. 149 (1964); Thorpe v. Housing Authority of Durham, 393 U.S. 268 (1969). The contracts involved in these appeals do not provide for the calculation of fair and reasonable profit in accordance with the weighted guidelines or any other ASPR profit guidelines. Appellant's entitlement to the application of "guidelines" springs from the direction of the Court of Claims in remanding this matter to the Board. In Lockheed Aircraft Corporation v. The United States, Ct. Cl. No. 46-65 (Decided May 15, 1970), the Court characterized the ASPR profit guidelines discussed by it in Newport News and Bethlehem as ". . . changes in procedural requirements and standards during the determination of a claimant's substantive rights." (Slip Op. p. 9; emphasis by the Court)

Appellant correctly points out that in Lockheed, the Court characterized its Newport News and Bethlehem decisions as favorable to, or for the benefit of the

claimant. (See p. 9, text and footnotes 7 and 9) Appellant contends that unless the weighted guidelines are applied it would be deprived of the profit to which it believes itself entitled. However, there is no indication that in Lockheed, the Court was referring to the application of one set of ASPR profit guidelines as distinguished from another. In Bethlehem, the Court expressed its awareness that the profit to which appellant might be found entitled on application of even the weighted guidelines could be less than the profit originally determined by the Board. What was "favorable" to appellant in the Bethlehem decision was the Court's determination that "guidelines" must be applied to determining profit, as distinguished from no guidelines at all.

In considering the "feasibility" of the weighted guidelines the ASPR Committee stated that they "effected a substantive change in the standards existing at the time the contracts were entered into . . . ." (Emphasis supplied) However, we have no basis to conclude that the ASPR Committee was attempting to dictate the ultimate result which the Board might reach in further proceedings on the merits. As stated previously, the Court left the determination of feasible standards to the authorized Department of Defense policy makers. Appellant points to indications that the actions of the ASPR Committee were specifically intended for application to the Board's resolution of these appeals, even though contracts not involved here were also considered. But such specific applicability was foreseen by the Court

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when it referred to the possible infeasibility of applying the weighted guidelines to the "instant contracts." The non-weighted guidelines are published guidelines of general applicability prior to 1964. They were regarded by the Court as acceptable for resolution of the Newport News controversy. The Court did not determine that appellant was entitled to any particular profit, and we accordingly do not regard the application of the non-weighted guidelines to resolution of the instant controversy as impairing appellant's vested rights in the sense meant by the Court.

We conclude that we are bound pursuant to the Court's directive, as implemented by the ASPR Committee, to apply the non-weighted guidelines, and not the weighted guidelines, in determining the profit to which appellant may be entitled. Appellant has contended that such a course of action would be improper for a number of reasons. We have considered appellant's objections in the context of determining the manner in which the Court has directed us to proceed. In opposing the Government's Motion appellant has in large part taken issue with the propriety of the course of action suggested in the penultimate paragraph of the Court's opinion. Our decision herein would, of course, be subject to change upon order or clarification rendered by the Court.

For the foregoing reasons the Government's Motion is granted. Appellant is ordered to inform the Board within 30 days as to whether it intends to make application to the Court for review of

this interlocutory ruling. If appellant does not intend promptly to make such application, the Board will issue instructions to the parties regarding further proceedings on the merits of these remanded appeals.

Dated 23 December 1970.

Daniel M. Arons
DANIEL M. ARONS
Member of Division No. 5
Armed Services Board of
Contract Appeals

I Concur

B. Lee Bird
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Member of Division No. 5
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I Concur

William J. Ruberry
WILLIAM J. RUBERRY
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I Concur

Richard C. Solidakke
RICHARD C. SOLIDAKKE,
Chairman
Armed Services Board of
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Member of Division No. 5

I Concur

Harris J. Andrews, Jr.
HARRIS J. ANDREWS, Jr.,
Vice Chairman
Armed Services Board of
Contract Appeals and
Member of Division No. 5

I certify that the foregoing is a true copy of the opinion and decision by the Armed Services Board of Contract Appeals in ASBCA Nos. 10316 and 10317 (Reinstated), appeals of Bethlehem Steel Corporation, rendered in conformance with the Board's Charter.

Dated: 13 January 1971.

George L. Hawkes
GEORGE L. HAWKES, Recorder
Armed Services Board of
Contract Appeals

IN THE UNITED STATES COURT OF APPEALS

No. 44-68

BETHLEHEM STEEL CORPORATION

v.

THE UNITED STATES

Before LARAMORE, Acting Chief Judge, DURFEE, DAVIS, COLLINS, SKELTON and NICHOLS, Judges.

O R D E R

This case comes before the court on plaintiff's motion, filed May 10, 1971, for an order terminating stay and for other relief. Upon consideration thereof, together with the opposition thereto, without oral argument,

IT IS ORDERED that plaintiff's said motion for an order terminating stay and for other relief be and the same is denied.

BY THE COURT

JUDGE LARAMORE

Acting Chief Judge

JUL -1 1971

ARMED SERVICES BOARD OF CONTRACT APPEALS

Appeals of --	)	
	)	
Bethlehem Steel Corporation	)	ASBCA Nos. 10316 and 10317
	)	
Under Contract Nos. NObs-3556 and NObs-3648)		(Reinstated)

APPEARANCES FOR THE APPELLANT:

E. J. O'Brien, Esq.,
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Bethlehem Steel Corporation

Of Counsel:

George Vradenburg, III, Esq.
New York, New York

APPEARANCES FOR THE GOVERNMENT:

Samuel Pinn, Jr., Esq.
Counsel for the Naval Ship Systems Command
Morris Amchan, Esq.
Assistant Counsel

OPINION BY MR. ARONS

History of the Dispute.

These appeals have been reinstated following the decision of the United States Court of Claims in Bethlehem Steel Corporation v. United States, 191 Ct. Cl. 141 (1970), in which the Court held that the Board, when it initially decided these appeals, erred in failing to consider the provisions of the Armed Services Procure-

ment Regulation (ASPR) which the Court regarded as applicable to resolving the matters in dispute. In these appeals appellant seeks to recover the amount of labor and material cost escalation said to be due pursuant to Article 6 of the Special Provisions of the above contracts, under which appellant built five destroyers for the Navy at its shipyard located in Quincy, Massachusetts. (Appellant is sometimes referred to herein as "Quincy.") Under Article 6(f) of the Special Provisions appellant warranted that its price proposals and other data submitted in connection with negotiation of the contract,

> ". . . exclude any allowance for contingencies to cover the possibility of increased costs of performance for which provision for price adjustment is made in this Article."

In exchange for this warranty, other paragraphs of Article 6 provided for adjustment in the contract price to take account of inflation in labor and material costs during performance. However paragraph (e) of that Article further provided,

> "(e) The Contracting Officer may deny, in whole or in part, any upward adjustment in the contract price required under this Article if the Contracting Officer finds that such adjustment is not required, in whole or in part, to enable the Contractor to earn a fair and reasonable profit under this contract."

Delivery of the last of the five ships was accomplished in February 1958. On 5 January 1960 appellant submitted its formal claims for accrued labor and material escalation, computed in accordance with the formula

specified in Article 6. Under NObs-3556 appellant claimed a total of $3,347,500. Under NObs-3648 appellant claimed a total of $2,404,900. Without escalation appellant had earned profits of 3.0% under NObs-3556, which covered three vessels, and 2.35% under NObs-3648, which covered two vessels, computed as percentages of cost. With full escalation appellant would recover profits of 9.3% under NObs-3556 and 9.6% under NObs-3648, computed as percentages of cost.

In final decisions, both dated 18 August 1964, the contracting officer denied appellant's escalation claims, after determining, pursuant to Article 6(e), that no upward adjustment in the contract prices on account of labor and material escalation was required to enable appellant to earn a fair and reasonable profit under either contract. In making his determinations the contracting officer excluded from the cost based used in computing the profit percentages certain costs which he did not consider allowable under the contracts. By virtue of these exclusions the contracting officer determined that appellant had earned, without escalation, a profit of 4.6% of contract costs under NObs-3556, and a profit of 5.0% of contract costs under NObs-3648.

Appellant then appealed to this Board pursuant to the Disputes clause in both contracts. In a decision dated 16 June 1966 (66-1 BCA par. 5639) the Board sustained the appeals in part. It determined that the contracting officer's cost disallowances were improper, and that appellant was entitled to escalation sufficient to enable it to earn a profit of 5.0% of costs under both contracts, with the cost amounts previously disallowed included in the cost base. Under the Board's

decision, appellant was allowed to retain a $1,000,000 partial escalation payment ($500,000 under each contract) which the contracting officer had approved in December 1959. Appellant was allowed a further $564,151 under NObs-3556 and $376,028 under NObs-3648. Appellant was thus allowed total escalation of $1,064,151 under NObs-3556 and $876,028 under NObs-3648.

Appellant then brought an action in the Court of Claims seeking to recover the balance of the escalation claimed. In its decision, dated 20 March 1970, the Court did not allow any further escalation. However, it followed the precedent which it set in Newport News Shipbuilding & Dry Dock Co. v. United States, 179 Ct. Cl. 97 (1967), a case involving the same Article 6(e), and held that in determining a fair and reasonable profit under appellant's contract, the Board erred as a matter of law in not resorting to profit determination techniques or guidelines prescribed by applicable published regulations. In the original proceeding before this Board, neither party relied on profit guidelines prescribed in ASPR or elsewhere, and the Board did not specifically consider any regulatory guidelines in determining the profit to which appellant was entitled. No such guidelines were in effect in 1954, when NObs-3556 and -3648 were awarded. However, the Court decided, as it did in Newport News, that a proper determination of fair and reasonable profit required consideration of the applicable profit guidelines and suspended proceedings to enable the parties to obtain further fact findings in accordance with its opinion. The appeals were thereupon reinstated by this Board.

After the appeals were reinstated the parties engaged in a preliminary controversy

over which set of ASPR profit guidelines should be applied in deciding the appeals on their merits. On the basis of certain language in the Court of Claims' decision, appellant contended that the Court of Claims required application of the so-called "Weighted Guidelines" set forth in ASPR Section 3-808 effective 15 August 1963. The Government maintained that the Court did not require use of the Weighted Guidelines, but instead, allowed Department of Defense policy makers to establish the applicability of other guidelines if the Weighted Guidelines were not considered feasible for resolution of this dispute, provided that no impairment of vested rights was attempted. In June 1970, the authorized Department of Defense policy making body, the ASPR Committee, determined that the so-called "non-weighted guidelines," set forth in ASPR Section 3-808 effective January 1960 should be considered applicable. The application of the non-weighted guidelines had been required by the Court for resolution of the Newport News litigation. The Government accordingly urged that the non-weighted guidelines should similarly be applied for disposition of the present appeals. For the reasons stated in our decision on the guidelines controversy, dated 23 December 1970 (71-1 BCA par. 8640), we agreed with the Government.

Appellant then filed a motion in the Court of Claims seeking termination of the suspension of proceedings and other relief. Appellant contended that the Board's decision on the guidelines controversy was erroneous. In an unpublished order dated 1 July 1971, the Court denied appellant's motion without stating any view as to which set of guidelines should be applied in deciding these appeals on their merits. Our disposition

of these appeals herein is accordingly governed by application of the non-weighted guidelines to the relevant facts. By agreement of the parties the specific text of the guidelines under consideration is that which appeared in ASPR Section 3-808 as of November 1962.

With the permission of the Board, appellant submitted for the record an offer of proof as to profit it considers itself entitled under application of the weighted guidelines. Appellant's offer of proof is not in evidence. With respect to appellant's insistence upon application of the weighted guidelines we note the memorandum dated 13 June 1963 by the Assistant Secretary of Defense for Installations and Logistics which indicated that the substitution of the weighted for the non-weighted guidelines was intended to quantify existing policy but not to introduce any drastic changes. That memorandum was quoted from extensively in our decision in Newport News Shipbuilding & Dry Dock Company, ASBCA No. 6565 (Reinstated), 71-1 BCA par. 8705, the decision on the Newport News appeal which followed the decision of the Court of Claims in Newport News Shipbuilding and Dry Dock Company v. United States, supra.

To a considerable extent the facts relevant to deciding these appeals have already been recited in the Board's original decision and in the opinion of the Court of Claims. In the original proceeding before this Board no evidentiary hearing was held; but the parties executed a lengthy stipulation of facts which was reproduced in toto in the Board's decision. Several exhibits were attached to the stipulation. After the appeals were reinstated, and following resolution of the guidelines controversy, a

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seven-day evidentiary hearing was held and numerous additional documents, obtained through mutual discovery, were submitted for the record. The record now consists of the materials originally before the Board, which were also before the Court, supplemented by the hearing transcript and additional documents submitted following reinstatement of the appeals.

At the hearing in the reinstated appeals the Government stated that in its view the amount of escalation allowed by the Board in its original decision resulted in a profit to appellant which was within a fair and reasonable range upon application of the non-weighted guidelines. Accordingly the Government does not now contend that the amount of escalation previously allowed by the Board should be reduced. (Tr. 1-111, 2-7; Govt. Brief, p. 8) The amount now in dispute is thus determined as follows:

	NObs-3556 (ASBCA No. 10316)	NObs-3648 (ASBCA No. 10317)
Accrued escalation	$3,347,000	$2,405,000
Escalation allowed per Board's original decision	1,064,151	876,028
Difference now claimed	$2,282,849	$1,528,972
Total claimed		$3,811,821

The Guidelines.

ASPR Section 3-808, entitled "Profit or Fee," in effect as of November 1962, included nine individual guidelines. They

were prefaced by the following introductory paragraphs:

"3-808.1 General. A fair and reasonable provision for profit or fee cannot be made by simply applying a certain predetermined percentage to the cost estimate or selling price of a product. Rather, the profit or fee should be first established as a dollar amount, after considering the factors set forth in this 3-808. Therefore, where a fee is involved and it is necessary to determine the percentage relationship between the fee and the estimated cost of the contract in order to comply with administrative and statutory limitations on fees for cost--reimbursement type contracts, the percentage shall be determined only after the dollar amount of the fee has been established for negotiation purposes.

"3-808.2 Factors for Determining Fee or Profit. The factors set forth in subparagraphs (a) through (i) below should be considered in determining profit or fee in all contracts, whether for supplies or services; for construction work; or for experimental, developmental, or research work, and whether of the fixed-price type or of the cost-reimbursement type unless otherwise specified in the particular factor. All of the following factors, as set forth in (a) through (i) below should be evaluated in the light of the basic policy set forth in 3-801.1 which provides that supplies and services shall be procured from responsible sources at fair and reasonable prices calculated to result in the lowest overall cost to the Government:

* * *

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We now turn to consideration of the individual guidelines, as applied to the relevant facts. The order of the following discussion reflects the order in which the guidelines are set forth in ASPR Section 3-808.

Factor (a) - Effect of Competition. This factor is stated as follows:

> "When competition is effective and proposals are on a firm fixed-price basis, the contracting officer normally need not consider in detail the amount of estimated profit included in a price. When effective competition is lacking, and in all cases where cost analysis is performed in accordance with 3-807.2(c) the estimate for profit, target profit or fee, or the proposed fixed fee should be analyzed in the same manner as all other elements of price, evaluating the factors set forth in this paragraph 3-808." 1/

The DD 931 Program.

The destroyers built by appellant under NObs-3556 and NObs-3648 were five of eighteen destroyers in the DD 931 class. Table I which follows indicates the pattern in which contracts were awarded for ships within that class:

1/ ASPR 3-807.2(c) prescribes techniques for performing a cost analysis. Neither party has relied on this subparagraph and we do not consider it material to the disposition of these appeals.

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TABLE I

Ship (Hull No.)*	Contractor	Contract Number	Date of Award
DD 931, 932, 933	Bath Iron Works	NObs-3371	15 December 1952
DD 936, 937, 938	Bethlehem Steel Corp.	NObs-3556	3 February 1954
DD 940, 941, 942	Bath Iron Works	NObs-3615	30 July 1954
DD 943, 944	Bethlehem Steel Corp.	NObs-3648	26 October 1954
DD 945, 946, 947	Bath Iron Works	NObs-3760	27 January 1956
DD 948, 949	Ingalls Shipbuilding	NObs-3761	27 January 1956
DD 950, 951	Puget Sound Bridge and Dredging Co.	NObs-3762	27 January 1956

* No contracts were awarded for hull numbers 934-5 and 939.

Preparation of Proposal.

As indicated by Table I, NObs-3556 required appellant to build the DD 936, DD 937 and DD 938 which constituted the second group of three ships in the DD 931 class. The requests for proposals ultimately leading to award of NObs-3556 were issued by the Navy Bureau of Ships on 21 October 1953 and 15 January 1954. Eight shipyards were invited to submit proposals. Of those eight, the following yards submitted proposals in the amounts indicated (rounded off to the nearest $1000):

TABLE II

Bath Iron Works	$15,492,000	each of three
Newport News	16,800,000	" " "
Bethlehem-Quincy	18,674,000	" " "
New York Shipbuilding	19,234,000	" " "

These amounts did not include contingencies for inflation. (Exh. A-2) Appellant also submitted an alternative proposal in the amount of $15,559,000 per ship conditioned upon award to it of a contract for the aircraft carrier CVA-61. The contract for the CVA-61 was awarded to Newport News on 3 February 1954, and was the contract out of which the Newport News litigation arose. Appellant considered its proposal for the CVA-61 high and noncompetitive since a carrier of that size could not be entirely built within the confines of the Quincy yard. (Tr. 2 - 59-60) Appellant's alternative proposal for the DD 936-8 was not considered by the Bureau of Ships.

At the time proposals were submitted

with respect to the DD 936-8, the prospects for future orders placed with American shipyards were considered bleak. (Exh. A-7) As a result of this business outlook the competition for available orders was intensified. (Tr. 2-19, 2 - 49-50) When appellant prepared its proposal it was aware of the workloads in other yards. Most signficantly it was aware that Bath Iron Works (hereafter "Bath") had been awarded NObs-3371, the contract which covered the DD 931-3. In appellant's view Bath had a considerable competitive advantage in bidding on the DD 936-8 by virtue of its experience under NObs-3371 involving similar ships.

Bath had submitted the low proposal for the DD 931-3 and was awarded NObs-3371 on 15 December 1952 at a price of $15,425,000 per ship subject to escalation and excluding the cost of design work. As the "lead yard" for the DD 931 class of ships Bath, in preparing its DD 936-8 proposal, did not have to include the cost of jigs, fixtures, scaffolding, etc. acquired for performance under NObs-3371 and which could be reused in constructing the DD 936-8. Furthermore in performing under NObs-3371, Bath's labor force acquired certain skills in constructing the first three DD 931 class ships which could be readily employed in the construction of follow-on ships within the same class. Bath thus had the advantage of a "learning curve" effect in preparing its proposal for the DD 936-8. (Tr. 1-53, 3 - 120-3) Furthermore delivery of the first of the three NObs-3371 vessels was not required until 1 November 1955. (Exh. G-6) Appellant was thus aware that in computing a per ship price for the DD 936-8, Bath was able to take its work under NObs-3371 into account in allocating fixed overhead. Appellant was similarly aware that Newport

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News, another of its competitors, would most probably receive award of the contract for the CVA-61, which would permit a lower per ship overhead allocation by Newport News in computing its price for the DD 936-8.

In contrast with Bath and Newport News, appellant's workload was rapidly dropping off. Delivery of vessels then on order was to be completed by October 1954. Without new orders, the Quincy yard would have no shipbuilding work as of October 1954. Appellant estimated an irreducible overhead of about ten million dollars a year for maintaining the Quincy yard in a state of readiness. (Tr. 1-23) Construction of the DD 936-8 would take up approximately five percent of the capacity of the Quincy yard. Appellant did not anticipate other future business which might absorb part of the fixed overhead. Accordingly, in preparing its proposal for the DD 936-8, appellant included overhead dollars of $4,901,000 per ship, or 107% of direct labor. (Exh. A-2) In contrast, the proposal submitted by Bath for the DD 936-8 included overhead at 97% or $2,667,136 per ship (Exh. A-2). Furthermore, the overhead dollars included in appellant's proposed price for the DD 1936-8 represented only about two-thirds of the total overhead that would have to be allocated to the DD 936-8 if no other business materialized during the construction period. In an effort to be competitive, appellant included in its proposed price overhead for only the first 27 months of an anticipated 38-month construction period. (Tr. 1-22, 24; ASBCA No. 10316, Rule 4, Tab 2) From the evidence presented we find that the disparity between the Bath and Quincy prices for the DD 936-8

was principally attributable to the comparatively large amount of overhead which appellant considered as having to be absorbed by the construction of the DD 936-8. We further find that appellant's proposed price was competitive in the sense that its preparation took into account appellant's dire need for new business, the lead yard advantage gained by Bath under NObs-3371, and the relatively favorable overhead projections prevailing for Bath and Newport News.

Award of NObs-3556.

During the negotiations which followed the submission of its proposal for the DD 936-8, appellant informed the Navy representatives that due to the absence of orders for future ship construction, the closing of the Quincy yard was imminent. The Navy representatives offered to award appellant the contract if appellant were to reduce its proposed price by one million dollars per ship. Appellant agreed to the concession and was awarded the contract at a price of $17,674,000 per ship. At this price appellant's estimated profit was $698,000 or about 3.7% of cost. (Exh. A-2) In appellant's view it was confronted with the choice of accepting the award on the terms offered by the Navy or closing the Quincy yard. (Tr. 1-34) Even with the price reduction, the Navy agreed to pay appellant, under the contract, a price for the three ships which was $6,546,000 greater than the price proposed by Bath. From the evidence presented we find that during the negotiations there was no specific discussion relating to the profit, if any, which appellant might reasonably earn under the contract, nor was there any specific discussion

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relating to the amount of escalation which appellant might recover under Article 6.

The basis for the Navy's decision to award the contract for the DD 936-8 to appellant was explained in hearings conducted on 26 February, 22 March and 29 March 1954 before the U.S. House of Representatives, Committee on Armed Services, Subcommittee on Defense Activities. Navy representatives who testified at those hearings included Mr. Robert B. Anderson, then Secretary of the Navy, and Rear Admiral Wilson D. Leggett, Jr., then Chief, Bureau of Ships. On the basis of their testimony we find that the Navy awarded NObs-3556 to appellant in order to assure the continued operation of the Quincy yard as a part of the mobilization base for ship construction. In making this decision, the Navy recognized that appellant's Central Technical Department, located at the Quincy yard, included personnel experienced in ship design and construction, the dissipation of which would be detrimental to the national security. The maintenance of the Central Technical Department contributed in some measure to appellant's overhead disadvantage vis-a-bis Bath. (Tr. 5-12; 13; Exh. A-1, A-2) The Navy also recognized that the Bethlehem yards represented about sixty percent of the Navy's commercial mobilization potential for surface combatant types of escort size vessel and above. In deciding not to award the contract to Bath, the Navy considered that as of 1 January 1954, employment at Bath was rising and that Bath had work on its books until 1956. Moreover, in deciding not to award the contract to Newport News, which had submitted the second lowest proposal, the Navy took into account the contemporaneous award of the carrier CVA-61 (RANGER) to that yard.

In awarding the DD 936-8 contract to appellant the Navy was adhering to a well-established policy of allocating ship construction work to various yards in order to maintain a balanced and widely dispersed mobilization potential.

Award of NObs-3648.

By letter dated 29 July 1954, the Bureau of Ships requested appellant to submit a proposal for the construction of the DD 943 and 944. Appellant submitted a proposal in the amount of $17,071,500 per ship, about $600,000 per ship lower than that price established in NObs-3556. The difference was attributable to the learning curve effect on direct labor output which was anticipated by appellant. (Tr. 2 - 109-10) For the DD 943 and 944 appellant estimated 1,762,000 labor hours per ship, while NObs-3556 was based on a labor estimate of 1,903,000 hours per ship. Appellant's proposal included $4,450,000 for overhead, or 104.4% of direct labor. (Exh. A-1) No other proposals were solicited or submitted with respect to the DD 943-4. At the time appellant was invited to submit a proposal for construction of the DD 943-4, the construction of the DD 940-2 was allocated to Bath under NObs-3615 at a price of $15,492,320 per vessel, the price per ship in the Bath proposal for construction of the DD 936-8. (Tr. 6-35; Ex. A-11)

In negotiations which followed the submission of appellant's proposal, Navy representatives maintained that appellant had overstated its overhead by failing to take adequate account of the nearly contemporaneous construction of the DD 936-8. The Navy offered a price of $16,250,000 per ship based upon estimated overhead of

$3,780,000, or 88.7% of direct labor. (Exh. A-1) Appellant accepted this offer, and NObs-3648 was awarded to appellant at that price. A breakdown of the contract price shows an estimated profit to appellant of $698,000 per ship, or 4.5% of cost without escalation. Although appellant was the only source solicited for the DD 943-4, its proposal, and the contract price agreed upon, reflected the competitive considerations and the need for additional business which were taken into account in the preparation of its previous DD 936-8 proposal. However, the award was again made to appellant pursuant to the Navy policy of allocating ship construction work to various yards.

Award of Contracts for DD 945-51.

The three contracts covering these seven vessels were all awarded following a single solicitation. As indicated above in Table I, NObs-3760, covering the DD 945, 946, and 947, was awarded to Bath. According to a Navy recap of proposals received, prepared prior to award, the following prices subject to escalation were proposed for each of three vessels (Exh. G-10):

TABLE III

Bath	$16,280,070
Bethlehem - Quincy	16,440,000
Bethlehem - Staten Island	16,580,000
Bethlehem - San Francisco	16,784,000
Ingalls	16,528,000
Newport News	16,950,000

According to the Bethlehem - Quincy proposal dated 28 December 1955 (Exh. A-25), appellant's proposed price subject to escalation for each of three vessels was $16,047,000. However, construction of the DD 945-951 entailed some significant revisions to working plans then being used for construction of previous DD 931 class vessels. The Bethlehem - Quincy proposed price did not include the cost of such plan revisions which appellant proposed to accomplish as design agent for all yards receiving awards for construction of the DD 945-51. Appellant estimated the cost of design services, including fee to be $834,600.

The evidence does not clearly indicate the reason for the difference between the ship construction price shown in appellant's proposal and appellant's price as shown in the Navy recap. However, the Navy recap was prepared for the purpose of comparing the various proposed prices. Under the terms of the Invitation for Bids, proposed ship construction prices were to include the cost of plan work. (Exh. G-20) The internal Navy memorandum prepared as a basis for making the award (called a business clearance) indicates that, for evaluation purposes, the cost of plan work was added to the proposals submitted by Bethlehem - Staten Island, and Bethlehem - San Francisco. (Exh. G-20) On the basis of these adjustments we infer that the Bethlehem - Quincy price, as shown on the Navy recap, also includes an adjustment for the cost of plan work in order to render that price comparable to the prices submitted by other yards.

Also as indicated in Table I above, NObs-3761, covering the DD 948 and 949, was awarded to Ingalls Shipbuilding Corporation; and NObs-3762, covering the DD 950

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and 951, was awarded to Puget Sound Bridge and Dredging Company. According to the Navy recap of proposals received (Exh. G-10), the following prices subject to escalation were proposed for each of two vessels:

TABLE IV

Bath Iron Works	$17,152,080
Bethlehem - Quincy	16,769,500
Bethlehem - Staten Island	17,377,000
Bethlehem - San Francisco	16,784,000
Ingalls Shipbuilding	16,873,440
Puget Sound	16,800,000
Newport News	17,546,000

The Bethlehem - Quincy proposal (Exh. A-25) quoted a price of $16,600,000 for each of two vessels. We again infer that for purposes of evaluation the Navy adjusted the Bethlehem - Quincy price to take account of the cost of plan work.

The contract prices subject to escalation for the DD 945-51 were as follows:

TABLE V

NObs-3760 (DD 945, 946, 947)- $16,223,000 per ship

NObs-3761 (DD 948, 949) - $16,225,000 per ship

NObs-3762 (DD 950, 951) - $16,445,000 per ship

On the basis of the above tabulation of proposals and the business clearance document

(Exh. G-20), we find that in making these awards, the relative proposed prices were taken into account, but that the controlling consideration was the Navy policy of distributing work among various yards and geographic locations.

In awarding contracts for the DD 945-51, the Bethlehem - Quincy proposal was not considered at all. At the time the Navy solicited proposals for these destroyers, it also solicited proposals for two frigates, DL 7 and 8. Ships in the DL class were larger and more powerful than the DD 931 class destroyers. (Tr. 3-64, 141) Appellant submitted the lowest proposal for the DL 7 and 8. Bath already had a letter contract for the DL 6, but the price proposed by Bath for the DL 6 was considered to be high. Accordingly, appellant was requested to submit a proposal for the DL 6. A comparison between the Bath and Quincy proposals indicated that Bath's proposed price, including plans for the DL 6, 7 and 8, was approximately $16,000,000 higher than the price proposed by Quincy. Accordingly the letter contract with Bath for the DL 6 was terminated and appellant was awarded NObs-3759 for the construction of the DL 6, 7 and 8. In the Navy's view, the award of this contract to appellant precluded consideration of appellant's DD 945-51 proposal. Appellant ultimately suffered a loss of $3,990,000 under Nobs-3759. (Exh. A-6; Tr. 4-53)

Escalation Allowed Under Contracts for DD 931 Class Vessels.

From the evidence presented we have constructed the following table which indicates the amount of escalation

allowed under each of the contracts for DD 931 class vessels and the impact of the escalation allowances on profits earned under those contracts:

DD No.	Yard	Actual Cost of Construction	Profit Before Escalation		Accrued Escalation	Escalation Allowed	Profit After Escalation	
			Dollar Amt.	% of Cost			Dollar Amt.	% of Cost
931-3	Bath	$43,944,313	$3,612,735	8.35	$3,077,884	ALL	$6,690,619	15.2
936-8	Quincy	53,204,600	1,596,079	3	3,347,000	$1,054,151	2,660,230	5
940-2	Bath	42,814,770	7,073,000	16.52	2,807,816	NONE	7,073,000	16.52
943-4	Quincy	33,028,700	775,407	2.35	2,405,000	876,028	1,651,435	5
945-7	Bath	43,736,052	6,079,948	13.9	1,931,385	622,360	6,702,308	15.32
948-9	Ingalls	34,653,639	(1,884,247 loss)	(5.4)	2,637,279	ALL	753,032	2.17
950-1	Puget Sound	31,777,709	1,135,119	3.6	2,080,471	ALL	3,215,590	10.1

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The escalation allowances shown above were made by the contracting officer under NObs-3371 (DD 931-3), NObs-3760 (DD 945-7), NObs-3761 (DD 948-9), and NObs-3762 (DD 950-1). The escalation allowance shown for Quincy reflects the result of the Board's original decision in these appeals.

Where escalation was allowed by the contracting officer, the reasons for the allowance were stated in a business clearance document. The allowance of full escalation under NObs-3371 was based in large measure upon the fact that Bath had submitted the lowest competitive price. (Exh. A-14a) Similarly the allowances of full escalation under NObs03761 (DD 948-9) and 3762 (DD 950-1) were justified on the ground that these contracts were awarded on the basis of competition. (Exh. A-18, A-20) The allowance of partial escalation to Bath under NObs-3760 was also justified on the ground that the award was obtained through competition. (Exh. A-16) Escalation was denied under NObs-3615 on the ground that payment of escalation would result in an unreasonably high profit to Bath. (Exh. A-15, G-14) Bath withdrew its escalation claim under NObs-3615 on 26 August 1960, when it became aware that partial escalation would be allowed under NObs-3760 (DD 945-7). Although factors such as competition, risk and performance were considered in determining the escalation allowed in 1960 under NObs-3760, 3761 and 3762, there is no evidence that profit guidelines prescribed by ASPR were specifically taken into account.

CONCLUSIONS UNDER FACTOR (a)

In our decision on the reinstated Newport News appeal we found as a fact

that "the award of the RANGER contract was the result of 'adequate and effective' competition." This finding was based in large part on evidence establishing that the award was made to Newport News because the difference between its proposal and the next higher proposal (that of Bethlehem - Quincy) was approximately $28,000,000. On the basis of this finding we stated the following conclusions as to the application of Factor (a) (71-1 BCA at 40,453-4):

> "We have found that competition in this instance was adequate and effective within the meaning of Factor (a), and are of the opinion that such being the case, attendant extrinsic conditions, efficiencies or inefficiencies, and agreed contract conditions such as the present provisions for escalation, must be allowed to operate without the intrusion of judgments of reasonableness based on other considerations. In short, it is our view that under Factor (a), what is fair and reasonable is determined by the consequences of competition and cannot be redetermined under article 6(e) of the contract. In our view, by operation of Factor (a), appellant is entitled to escalation to the full extent permitted by article 6 of the special provisions."

In Newport News, the Board thus allowed full escalation through application of Factor (a) alone, although in an alternative holding the Board also considered Newport News entitled to full escalation through application of the other eight guidelines.

Appellant contends that the awards of both NObs-3556 and Nobs-3648 were based on competition, pointing to the influence

of competitive factors on the preparation of its respective proposals. Appellant says that the competition for the award of NObs-3556 was more severe than the competition considered in Newport News. According to appellant, the Court in Newport News considered the Bethlehem - Quincy proposal for the CVA-61 to be competitive when in reality it was not competitive. Appellant further notes that competitive pressure enabled the Navy to insist upon $1,000,000 per ship discount as a condition to awarding appellant a contract for the DD 936-8, which further increased the disparity between appellant's proposal and estimated costs.

We agree with appellant to the extent that the prices for the DD 936-8 and 943-4 reflected competitive influences. However, as indicated by ASPR 3-808.2, quoted above, Factor (a) must be read in the light of the basic policy which provides that supplies and services shall be procured from responsible sources at fair and reasonable prices calculated to result in the lowest overall cost to the Government. Had this basic policy been observed, NObs-3556 would have been awarded to Bath. Although effective competition was present in this procurement the overriding basis for making this award was not the result of such competition. The award was made as the result of the Navy's decision to assure continued existence of appellant as a part of the mobilization base, and further pursuant to the Navy's policy of allocating its ship construction work among various yards. The award of NObs-3648 similarly resulted from the Navy's policy of allocation. Considerations of price played only a secondary role in determining the award of these contracts to appellant. In the case of NObs-3556,

it is clear that the Government paid considerably more than if the award had been made strictly as the result of price competition. The circumstances of the awards to appellant thus differed materially from the circumstances which we found in Newport News to justify full escalation under Factor (a).

Appellant further contends that in determining whether it is entitled to additional escalation under Factor (a), we should take account of the escalation allowed under other contracts for DD 931 class vessels. Appellant urges particularly that we consider the escalation allowed under NObs-3760, 3761 and 3762 covering the DD 945-51. Appellant submits that the escalation under those contracts was allowed by the Navy on the ground that the awards were obtained by competition, although appellant had submitted the lowest proposed price. The most striking comparison to be drawn is that Bath was allowed sufficient escalation to enable it to earn a $6,702,308 profit for three vessels under NObs-3760, whereas appellant, with the escalation allowed by the Board, earned a $2,160,230 profit for three vessels under NObs-3556. Appellant insists that if the award of NObs-3760, 3761 and 3762 were based on competition, the relatively low escalation allowed appellant under NObs-3556 and 3648 amounts to an unfair discrimination.

We have doubts as to the relevancy of appellant's reliance upon the escalation allowed under NObs-3760, 3761 and 3762 to the aplication of Factor (a) in the present appeals. Factor (a) is addressed to the extent of competition

prevailing in an individual procurement, not to competition which might prevail in future procurements. Furthermore, Factor (a), along with the other factors, are couched in terms of considerations to be taken into account by a Government negotiator when negotiating an individual contract. As stated in ASPR 3-807.8, in effect as of 26 November 1962, "Each contract shall be priced separately and independently, and no consideration shall be given to losses or profits realized or anticipated in the performance of other contracts."

Even if the extent of competition which prevailed in the award of NObs-3760, 3761 and 3762 is relevant to the application of Factor (a) in these appeals, the facts do not support appellant's contention that the Navy has unfairly discriminated against it. The Navy's decision to award the contracts for three vessels to Bath, two vessels to Ingalls, and two vessels to Puget Sound, with appellant obtaining the award for three DL's, reflected the Navy's policy of allocation. However, as discussed above, appellant was apparently not the low bidder if the cost of plan work is taken into account. Even if the inference which we drew from the evidence in this regard is erroneous, the differences between appellant's proposed prices and the prices proposed by Bath, Ingalls and Puget Sound for the DD 945-51, indicated in Tables III and IV above, were small compared with the disparity between appellant's and Bath's prices for the DD 936-8, even with the $1,000,000 reduction in the price per ship reached during appellant's negotiations with the Navy. Appellant's reliance upon the circumstances leading to

the award of NObs-3760, 3761 and 3762, and the escalation eventually allowed thereunder lacks substantial merit.

We conclude that NObs-3556 and 3648 were awarded on the basis of considerations other than the results of price competition. In view of the disparity between appellant's proposed price for construction of the DD 936-8 and the lowest proposed price, that of Bath, we further conclude that appellant is not entitled to additional profit under NObs-3556 on the basis of Factor (a) alone. Since the award of NObs-3648 did not involve competition between various yards, and was based solely on the Navy's decision to allocate the DD 943-4 to Quincy, appellant is not entitled to additional profit under NObs-3648 on the basis of Factor (a) alone. We must accordingly apply the other guidelines to the facts relevant thereto in order to determine whether appellant is entitled to additional profit.

Factor (b) - Degree of Risk. This factor is stated as follows:

> "(1) The degree of risk assumed by the contractor should influence the amount of profit or fee a contractor is entitled to anticipate. For example, where a portion of the risk has been shifted to the Government through cost-reimbursement or price redetermination provisions, unusual contingency provisions, or other risk-reducing measures, the amount of profit or fee should be less than where the contractor assumes all risk.
>
> "(2) Some cost-plus-a-fixed-fee contracts and task orders for research

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> and development call for the delivery of prototypes of other 'hardware.' Other such contracts or task orders require only that the contractor exert his 'best effforts' to deliver the required end item. Frequently this is because the contractor is not willing to assume the additional burden of incurring substantial cost overruns without additional fee in order to complete performance. When the contract calls for delivery of developed models in accordance with well-defined performance or design characteristics or a predetermined delivery schedule, or both, in contrast to an obligation only to exert his 'best efforts' to develop and deliver such models, payment of the fee should be conditioned on performance in accordance with the contractor's obligation to deliver, and in such cases the contractor may be entitled to a larger fee because of the risk inherent in his commitment and because of the successful completion of the work."

As stated by the Court of Claims in Newport News Shipbuilding and Dry Dock Co. v. United States, supra, this factor is to be applied prospectively, not with the benefit of hindsight. Thus we are to examine the risks assumed by appellant at the time it was awarded NObs-3556 and NObs-3648 without consideration of whether those risks eventually materialized.

Non-inclusion of All Anticipated Overhead Costs in Proposed Price.

As stated above, appellant's proposal for the DD 936-8 included approximately two-thirds of overhead anticipated

for the construction period on the assumption that no further business would materialize. Appellant's proposal for the DD 943-4 was prepared on the same basis. (Tr. 1-22) At the time appellant prepared its proposals for the DD 936-8, and DD 943-4 it had no reason to believe that it would receive substantial additional orders for ship construction. Its decision not to include full anticipated overhead in its proposals emanated from its belief that such an omission was necessary in order for it to be competitive. Appellant's proposed price for the DD 936-8 was further reduced by $1,000,000 per ship during negotiations. We find that at the time of award of NObs-3556 and 3648, appellant assumed more than the usual risk that anticipated costs would overrun the contract prices for the five ships, even allowing for escalation. Fortunately for appellant, it eventually obtained orders for tankers from oil companies following the 1956 Suez crisis, thereby expanding the direct cost base over which it could distribute its fixed overhead. (Tr. 3 - 64-8) However, the eventual mitigation of appellant's risk of loss under NObs-3556 and 3648 is irrelevant to our consideration of the risk which prevailed at the time of award.

Risk of Inadequate Lead Yard Plans.

Article 1(c) of the Special Provisions of NObs-3556 provided that:

> "(c) The Contractor may, at its own expense and at its election, obtain, at the cost of reproduction, copies of detail working plans, booklets, manuals, and other plans and data relating to the construction of Destroyers (DD931) from Bath Iron Works Corporation, Bath,

> Maine. The Government does not guarantee, nor does the Government make any representations with respect to, the timeliness of the delivery of such plans, booklets, manuals, and other data nor the correctness and accuracy of any details, dimensions or any other information shown on such plans, booklets, manuals and other data, nor does it guarantee that such plans, booklets, manuals and other data include all plans, booklets, manuals and other data necessary for the construction of the vessels."

The comparable clause in NObs-3648 provided in effect that appellant could use, at its election, the working plans, etc. relating to the construction of the DD 936-8. The clause included similar disclaimers as to Government responsibility for the accuracy of the plans, etc.

Under NObs-3371 (Exh. G-6), Bath, as the lead yard for the DD 931 class of destroyers, had the responsibility for preparing detail working plans, manuals, booklets, etc. However, NObs-3371 further provided that Bath would enter into an agreement with Gibbs & Cox, Inc., a highly-regarded naval architectural firm, for the preparation of working plans. (Tr. 5-12) The agreement with Gibbs & Cox was to be on a cost reimbursement basis, with the Navy reimbursing Bath for the allowable costs incurred by Gibbs & Cox. NObs-3371 stated the total estimated cost for performing such plan work at $6,967,500.00.

At the time appellant submitted its proposal for the DD 936-8, the working plans for the DD 931 were about 40 percent complete. (Tr. 5-39, 126) At the time

appellant was awarded NObs-3648, for construction of the DD 943-4, the working plans for the DD 931 were about 85 percent complete. (Tr. 5 - 41-2) Based on the testimony of the Government's engineering witness (Mr. Miller), who served as project engineer on the DD 931 program between 1957-9, we find that in general, a lead yard incurs a greater risk than a follow yard as to the adequacy of plans and working drawings. (Tr. 5-38) The DD 931 was in effect a prototype ship, the construction of which involved extensive engineering calculation and design work, and the ordering of major components which were being specified for the first time. (Tr. 5-8) Bath thus incurred the risk that inadequate lead yard plans might augment its construction costs in terms of rework and delay. However, Bath incurred virtually no risk with respect to the additional costs of architectural or engineering work necessary to revise inadequate plans or working drawings.

Appellant's proposal for the DD 936-8 was based on the assumption that the lead yard plans would be timely and adequate. (Tr. 2 - 99-100) Appellant's proposal included an estimate of 96,000 manhours for engineering. (Tr. 2-111) However, this estimate substantially represented the effort involved in reviewing and monitoring the lead yard plans. (Tr. 2-100) Lead yard plans can rarely be used by a follow yard without some adjustments. (Tr. 5-144) We are unable to find that appellant's proposal for the DD 936-8 included a substantial contingency for inadequate lead yard plans. For the DD 943-4, appellant estimated 130,000 engineering manhours, with the increase attributable to appellant's experience in working with the lead yard

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plans under NObs-3556. (Tr. 2-111)

NObs-3556 did not include any special provision for reimbursement of appellant's costs with respect to plan work. Appellant thus assumed the risk, under its fixed price contract, of both the cost of plan revisions necessitated by inadequate lead yard plans and attendant rework and delay costs. Under Article 1(c) of the Special Provisions, appellant was assured only of being able to obtain the lead yard plans as they became available. The Government disclaimed all responsibility for the timeliness or adequacy of the plans. That the timeliness and adequacy of lead yard plans has been a significant problem to follow yards is evident not only from the testimony of appellant's witnesses, but also from a Comptroller General's Report to Congress dated 28 February 1972 (Exh. A-31). In that report, late and inaccurate lead yard working plans are viewed as major sources of shipbuilders' claims. Aside from the merits of individual claims, the Navy has conceded the significance of the problem.

From the record presented as it relates to this matter we find that the risk assumed by appellant under NObs-3556 with respect to inadequate or untimely lead yard plans was substantial and roughly equal to the comparable risk assumed by Bath under NObs-3371. We base this finding principally on the non-existence of more than half of the lead yard plans at the time appellant submitted its proposal for the DD 936-8. We also take into account the risk assumed by appellant as a follow yard that the Navy Superintendent of Shipbuilding at Quincy might have views as to adequacy of plans different from those of

the Superintendent of Shipbuilding at Bath, Maine. (Tr. 3-126, 5-153) We further find that appellant's risk under NObs-3648 with respect to the timeliness or adequacy of lead yard plans was considerably reduced. However, its risk under that contract was still greater than the comparable risk assumed by Bath, Ingalls, and Puget Sound under NObs-3760, 3761, and 3762. The DD 931 was delivered in November 1955, prior to the award of those contracts. The contractor under NObs-3760, 3761 and 3762 had the benefit of a complete set of working plans on which corrections or follow-up actions had been made. They further had the benefit of knowing the results of the DD 931 acceptance trials. (Tr. 4 - 110-12, 5 - 40-41)

The DD 945-51 consisted of what Mr. Miller described as a sub-class of DD 931 class vessels in that the plans and specifications were reissued by the Bureau of Ships to include various changes that had been made. (Tr. 5 - 43-4) To some extent new working drawings had to be generated, although the record in these appeals does not reveal the extent of the changes. We are unable to find that the need for preparation of some new working drawings imposed a risk of plan unavailability or inadequacy upon the contractors under NObs-3760, 3761, and 3762 as great as the comparable risk imposed upon appellant under NObs-3556 or 3648.

Effect on Risk of Various Standard Contract Provisions.

In addition to the effect on risk of the relative adequacy and availability of lead yard plans, testimony and argument has been addressed to the question of

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whether certain provisions of the contract tended to reduce the risks otherwise imposed upon appellant. The clauses under consideration appear to be similar or identical to the comparable clauses included in NObs-3557, the contract for the CVA-61 (RANGER) awarded to Newport News, the contract under which the Newport News litigation arose. The effect of these clauses on a shipbuilder's degree of risk was discussed extensively in our opinion in the reinstated Newport News appeal.

The Escalation Clause.

The escalation clause referred to is Article 6 of the Special Provisions which has been discussed above. In the reinstated Newport News appeal we found that the escalation clause did not, as of the time of contracting, shift the entire risk of economic inflation of labor and material costs from the contractor to the Government. We considered that subparagraph (e) raised the specter of a protracted dispute even if the contractor eventually prevailed in overcoming an adverse determination under that clause. We also considered that Article 6 would not protect the contractor from actual material or labor cost increases exceeding the levels stated in the applicable Department of Labor Indices. We find, on the basis of testimony presented in the appeals now before us, that even in the absence of any dispute over escalation, payment of escalation under Article 6 is less prompt due to procedural delays, than in the case of a firm fixed price contract where the fixed price includes contingencies for inflation. (Tr. 4-13)

At the time NObs-3556 and 3648 were awarded, there was no discussion of whether the escalation clause would adequately protect appellant from the consequences of inflation. Appellant assumed that it would be protected by the applicable formulas. (Tr. 3-9, 10) Nevertheless the risk of inadequate protection still existed. Under subparagraph (d) of Article 6, appellant could ask the Navy to recognize another formula if the formula prescribed by the clause did not produce equitable results. However, subparagraph (d) imposed the risk that the Navy could not be so persuaded. The Government contends that the facts in the present appeals warrant a different conclusion from that reached in the reinstated Newport News appeal as to the implications of the escalation clause on risk. We are unable to find any meritorious distinctions in this regard, and accordingly conclude, as we did in Newport News, that the escalation clause did not entirely shift the economic risk of inflation from appellant to the Government.

Changes and Suspension Clauses.

These are Articles 4 and 16, respectively of both NObs-3556 and 3648. Identical clauses were commented upon in our opinion on the reinstated Newport News appeal. 2/ In Newport News, we concluded that at the time of contract award, the Changes and Suspension clauses did not tend to shift any substantial risk inherent in changes and suspensions from appellant to the Government.

The Government maintains that the

2/ These clauses were quoted in their entirety in the Appendix to the Board's decision in the reinstated Newport News appeal.

obligation imposed by these clauses upon the Government to negotiate equitable adjustments on a "sole source" basis in effect affords the contractor an improved remedy as compared with the common law remedy of bringing an action for breach of contract. According to the Government this improved remedy is risk reducing. This type or argument was considered by the Board in the reinstated Newport News appeal where we observed that when these clauses are read in conjunction with the standard Disputes clause, the contractor might lose bargaining power by having to execute a direction prior to price adjustment. We also observed that if the price adjustment claimed is contested, the contractor might suffer substantial delay and expense under the disputes procedure. Furthermore, as pointed out by appellant, the power of the Government to issue change or suspension orders under NObs-3371 imposed a risk upon appellant as a follow yard, dependent upon the timeliness and adequacy of working plans generated by Bath under NObs-3371. To some degree a follow yard assumes the risk that changes will be made in the lead ship with no comparable changes in the follow ship, although the Navy's more common practice was to direct changes in the follow ships which were not made applicable to the lead ships. (Tr. 5 - 140-1)

We conclude that the Changes and Suspension clauses included in NObs-3556 and 3648 did not have a risk reducing effect. If anything, the authority of the Government to change or suspend the work performed under NObs-3371 augmented the risk imposed upon appellant.

Insurance Clause.

Article 9 of the General Provisions of both NObs-3556 and NObs-3648 was the standard clause entitled "Insurance - Property Loss or Damage - Liability to Third Persons." This clause was commented upon in our decision on the reinstated Newport News appeal. In that decision we stated that:

> "Since the cost of insurance would not be a negligible expense if incurred on a project of this nature and size, we regard article 9 of the general provisions as tending to reduce the risk of such costs."

In its most relevant respect the Insurance clause provided (in subparagraph (a) thereof) that, unless otherwise directed by the Navy, the contractor was not to procure insurance against loss or damage to vessels or materials or equipment therein to the extent such risk of loss or damage would have been assumed by underwriters under standard marine builder's risk policies. The Government in effect became a self-insurer for such risks.

At the hearing in the appeals before us the vice-president who headed appellant's Shipbuilding Division (Mr. Strohmeier) testified that the Insurance clause adds to the contractor's risk since a shipbuilder can make more expeditious settlements with the commercial insurance industry than with the Government. He disagreed with the above quoted statement from our Newport News opinion, as it might be made applicable to the present appeals, on the ground

that the magnitude of risks involved in destroyer construction are readily insurable. (Tr. 3-28, 29) Mr. Strohmeier's testimony was not contradicted.

Notwithstanding Mr. Strohmeier's comments, the Insurance clause in effect transferred to the Government risks associated with obtaining insurance in the commercial market. For example, under the clause the contractor is not confronted with the risk of increases in insurance premiums during the course of construction. We accordingly find that the Insurance clause tends to be risk reducing. However, in view of Mr. Strohmeier's uncontradicted testimony as to the availability of commercial insurance and comparative experiences in making settlements, we further find that the Insurance clause has very little effect on the overall allocation of risks provided for in NObs-3566 and NObs-3648.

Limitation on Liability for Defects in Guaranty Period.

General Provision 6 of both NObs-3556 and 3648 provided in effect that appellant was liable for correction of defects discovered during the six month guaranty period following the date of preliminary acceptance of each vessel. However, Article 7 of the Special Provisions of each contract limited appellant's liability. For the three vessels to be delivered under NObs-3556 appellant's liability for such defects was limited to $265,110. For the two vessels to be delivered under NObs-3648 appellant's liability was limited to $162,500. When considering the effect of similar provisions in the reinstated Newport News appeal, we concluded for

the reasons stated therein, that the limitation on liability had a risk reducing effect. In the record now before us there is no basis to distinguish that conclusion. We accordingly conclude that the limitations on liability provided for in Article 7 of the Special Provisions of NObs-3556 and 3648 respectively had a risk reducing effect.

Government-Furnished Property.

The provisions in NObs-3556 and 3648 concerning Government-furnished property were generally similar to those discussed in our opinion in the reinstated Newport News appeal. Article 31 of the General Provisions was the standard Government-Furnished Property clause. Article 1(d) of the Special Provisions required the Government to furnish the materials listed on schedules (Schedule A) respectively attached to each contract. Under Article 8 of the Special Provisions the Navy was entitled to make changes in the list of materials.

In the reinstated Newport News appeal we concluded for the reasons stated therein that,

> ". . . the Government-furnished property arrangements in the contract did not tend to shift any major risk from the contractor to the Government and for present purposes were neutral in effect, the situation being analogous to that found . . . in connection with the changes and suspension clauses."

There is no basis in the record now before us to distinguish this statement. Accordingly we conclude that the Government-furnished property arrangements in NObs-3556 and 3648 did not have a risk reducing effect.

CONCLUSIONS UNDER FACTOR (b)

As indicated above, the manner in which the NObs-3556 price was determined, and the status of lead yard plans at the time of award, resulted in the assumption by appellant of greater than the normal risk of loss assumed by contractors for DD 931 class vessels. The risk assumed by appellant under NObs-3648 by reason of these factors was somewhat less, but was still greater than the norm. We further conclude that the various standard clauses having a possible impact on risk were either neutral in effect or had only a minimal effect on alleviating appellant's overall risk of loss. We accordingly determine that considerations under Factor (b) tend to support an allowance of additional profit to appellant.

Factor (c) - Nature of Work to be Performed. This factor is stated as follows:

> "A major consideration in the determination of the amount of profit or fee, particularly in connection with experimental, developmental, or research work, is the difficulty or complexity of the work to be performed and any unusual demands of the contract, such as whether the project involves a new approach unrelated to existing equipment or only refinements on existing equipment, whether the caliber or class of

engineer involved is that of an 'idea-man,' or whether the contractor is to be required by the contract to assign to the work unusually skilled talent."

Again the Court of Claims in Newport News Shipbuilding and Dry Dock Company v. United States, supra, indicated that this factor is to be applied prospectively, i.e., at the time of award.

Comparisons of DD 931 Class Vessels with RANGER.

Most of the evidence presented with respect to this factor involved a comparison in terms of relative complexity between the construction of the aircraft carrier RANGER, and the construction of a DD 931 class destroyer. In our decision on the reinstated Newport News appeal we found that ". . . the work to be anticipated under the RANGER contract was both difficult and complex within the meaning of Factor (c)."

Appellant's position is that the construction of a DD 931 class destroyer was more complex than the construction of the RANGER. In support of this position appellant's witnesses testified that the complexity or difficulty of constructing a ship is to be measured in terms of compactness or congestion. Although a destroyer is smaller than a carrier, relatively more material must be installed, and more activity performed, in each increment of space. Appellant's engineering witness (Mr. Mack-Forlist) testified that because of the size of the aircraft carrrier, materials can actually be stored on the ship, which facilitates scheduling and control of construction. Such storage is not possible on the destroyer. He cited various technical

factors such as the relatively high ratio of shaft horsepower to tonnage which, as compared with the carrier, resulted in an increase in the complexity of installing piping and electrical cable in the relatively small space allowed to accommodate these items. (Tr. 1 - 107-10, 2- 57,9, 3 - 3-8, 3 - 111-12, 4 - 59-63, 4 - 99-109)

The Government's engineering witness (Mr. Miller) testified that notwithstanding the compactness and close working areas in the destroyer, the DD 931 class vessel in no way approached the overall complexity of the RANGER from construction or design standpoints. He did not agree that Mr. Mack-Forlist's method of evaluation complexity in terms of relative congestion provided a valid overall analysis. Mr. Miller testified that the carrier was the more complex vessel to construct if one takes account of the comparatively large number of skilled workmen which had to be organized and supervised at any one time, the greater amount of material which had to be organized into a systematic flow, the many sophisticated systems on a carrier which were not required on a destroyer, and welding difficulties attributable to a type of steel used in a carrier which was not used in a destroyer. Mr. Miller further testified that the DD 931 class vessel was complex in terms of the quantity of engineering and the workmanship required to install various systems, but, such vessels were not as complex as others. (Tr. 5 - 28-32, 5 - 100-8, 5 - 112-24)

It is apparent that Mr. Mack-Forlist and Mr. Miller were employing somewhat different criteria for evaluating the relative complexity of the RANGER on the one hand, and the DD 931 class vessels on the other.

On the record presented we are unable to find that the DD 931 class vessels were more complex than the RANGER. We do find that the construction of DD 931 class vessels was difficult and complex within the meaning of Factor (c).

Comparison with Other DD 931 Class Vessels.

In considering the impact of Factor (c) on the disposition of these appeals, we further take into account the complexity of appellant's tasks under NObs-3556 and 3648, as compared with the complexity of the tasks confronting other contractors who undertook to construct DD 931 class vessels. It is noteworthy in this regard that the Navy allowed full escalation to Puget Sound under NObs-3762 partly on the ground that the work was considered complex. In view of the status of the DD 931 as a prototype ship, involving the installation of systems never previously employed, we find that the work performed by Bath under NObs-3391 was relatively more complex, within the meaning of Factor (c) than the work performed by appellant under NObs-3556 and 3648. In making this finding we do not overlook the specific exclusion from NObs-3371 of four items of work which were not similarly excluded from appellant's contracts. (Exh. G-6; Tr. 3 - 133-4, 3 - 143-4) We further find that the work performed by Bath, Ingalls and Puget Sound under NObs-3615, 3760, 3761 and 3762 was not more complex than that performed by appellant. Under Factor (c) an evaluation of relative difficulty or complexity involves consideration of new technical approaches or unusual technical problems. At the time of award of NObs-3556, the only prior experience available to appellant with respect to unusual technical problems affecting DD 931 class

vessels was Bath's partial experience in performing under NObs-3371. From this standpoint, the complexity of the task confronting appellant in performing under NObs-3556 was greater than that confronting the contractors under later contracts, including appellant under NObs-3648.

CONCLUSIONS UNDER FACTOR (c)

The Government contends that Factor (c) does not operate in appellant's favor on the ground that a s compared with the RANGER, or the DD 931, the vessels constructed by appellant did not involve experimental, developmental or research work, unusual demands, or a new approach unrelated to existing equipment. The Government had in effect espoused the position taken by its procurement specialist (Mr. Markowich) who, on the basis of his experience with shipbuilding contracts, testified that in his opinion the relative complexity of building a ship is diminished when the shipbuilder is experienced. (Tr. 6 - 24-5) Since appellant was an experienced shipbuilder, he considered that the degree of complexity in constructing the DD 936-8 and 943-4 was not very great.

We cannot adopt the Government's narrow interpretation of Factor (c) which would ignore the evidence establishing the overall complexity of building DD 931 class destroyers, and render Factor (c) operable only in situations where a contractor is to perform substantial research and development or some other extraordinary technical task. The language in the factor relied upon by the Government is intended to provide examples of work considered to be complex but it is not intended to be exclusive. Furthermore, in the Government's view an inexperienced

shipbuilder would be rewarded for performing a difficult task while an experienced shipbuilder would not be rewarded for performing the same task. We agree that a shipbuilder's experience is relevant to determining the degree of compexity of a given task confronting it at the time of award, but we do not agree that the element of experience controls the applicability of Factor (c).

We determine that Factor (c) tends to support an allowance of additional profit to appellant. We further find that because of the experience element, Factor (c) supports an allowance of additional profit under NObs-3556 more strongly than under NObs-3648.

Factor (d) - Extent of Government Assistance. This factor is stated as follows:

> "The Department of Defense encourages its contractors to perform their contracts with the minimum of financial, facilities, or other assistance from the Government. Where extraordinary financial, facilities, or other assistance must be furnished to a contractor by the Government, such extraordinary assistance should have a modifying effect in determining what constitutes a fair and reasonable profit or fee."

Facilities Assistance.

Effective 9 September 1940 appellant and the Navy entered into Contract NOd-1534 (Exh. G-7), a facilities contract under which appellant was to erect certain facilities for use in constructing ships eventually put to service in World War II. Under this contract appellant was obligated to maintain these facilities. This contract, as amended

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from time to time, was in effect when NObs-3556 and 3648 were awarded.

When appellant submitted its 14 November 1952 proposal for construction of the DD 931-3, it stated that the acquisition cost pf Government-owned facilities then in the Quincy yard was approximately $19,546,000. Appellant further stated that since these facilities were intermingled with its own facilities, it was unable to estimate the extent to which Government-owned facilities would be used to perform any resulting contract for the destroyers.

In performing under NObs-3556 and 3648 appellant found that it had to use certain facilities constructed under the facilities contract such as railroad tracks and water pipes, which were commingled with similar facilities erected at appellant's own expense. (Tr. 1-78, 3-80) However, the principal items erected under the facilities contract were a wet basin, lifting facilities, and an armor shop to be used in the construction of World War II type aircraft carriers and cruisers. (Tr. 6 - 55-8) From the evidence presented we find that those facility items were not usable for the construction of DD 931 class destroyers. (Tr. 1-78, 3-80, 6-58) Since the facilities contract required appellant to maintain and insure the facilities at its own expense, some of appellant's overhead expenses were incurred as a result of its responsibility under the facilities contract to maintain facility items having no utility in the construction of destroyers. (Tr. 6-58) The record in these appeals does not indicate the extent to which the overhead allocable to NObs-3556 and 3648 was attributable to appellant's

obligations under the facilities contract. For purposes of Factor (d) we find that the facilities erected at Government expense under the facilities contract did not amount to extraordinary Government assistance.

Financial Assistance.

NObs-3556 and 3648 both included the usual provisions for payments based on progress of the work less a reserve against any cost to the Navy of correcting defects developing during the guaranty period for which the contractor is held responsible. We find, as we did in the reinstated Newport News appeal, that the system of progress payments did not constitute extraordinary financial assistance from the Government within the meaning of Factor (d). 3/

As indicated in our discussion under Factor (a), NObs-3556 was awarded at a price of $2,182,000 per ship in excess of the per ship price offered by Bath for construction of the same vessels. For the three ships the total price difference was thus $6,546,000. NObs-3648 was awarded to appellant at a price of $758,000 per ship in excess of the Bath price for the

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3/ The evidence establishes that the Government withheld a reserve under NObs-3556 and 3648 of one to two percent greater than the reserve withheld under the comparable contracts with Bath, Ingalls, and Puget Sound. Appellant contends that this discrimination amounted to Government assistance in reverse. However, we do not consider this contention relevant to the application of Factor (d).

DD 936-8 on the basis of which NObs-3615 (for construction of the DD 940-2) was awarded. Assuming the validity of a comparison between the Bath proposal for the DD 936-8, and the award of NObs-3648 to appellant for construction of the DD 943-4, the difference between appellant's and Bath's prices for the two ships awarded appellant under NObs-3648 was $1,516,000.

In discussing the analysis which the Board is required to make in determining appellant's dependence on Government financial assistance, the Court of Claims stated the following in Bethlehem Steel Corporation V. United States, supra:

> ". . . If the dependence is great, it is a minus factor in determining the allowable profit. While the point may be debatable, we think that the addition of a bonus to a contract price to enable the contractor to maintain uneconomically large facilities in being is in reality a form of Government financial assistance and should be treated as such."

Although the Court referred in this connection to the relevant ASPR weighted guideline, we consider that its comment is equally pertinent to the application of Factor (d) in the non-weighted guidelines.

Appellant contends that the disparity between the award prices of appellant's two contracts and the comparable Bath prices should not be considered a bonus to appellant. Appellant points to the manner in which NObs-3760, 3761 and 3762 were awarded, and says that greater costs borne by the Navy as a result of its allocation policy constitute a portion of the cost of the national defense.

Appellant alludes in this regard to the Merchant Marine Act of 1936, as amended which, in 46 U.S.C. 1152, provides in part that:

> "In the event that a contract is made . . . for a price in excess of the lowest responsible bid which would otherwise be accepted, such excess shall be paid by the Secretary of Commerce as part of the cost of national defense and shall not be considered as a part of the construction-differential subsidy."

As found in our discussion under Factor (a) the paramount consideration dictating the award of NObs-3556 to appellant was the Navy's view that the Quincy yard had to be kept in operation for national security considerations. We thus agree with appellant that the disparity between the award price and the lowest proposed price was a cost borne by the Government in the interest of the national defense. However, it does not follow that this additional cost to the Government is irrelevant to a determination of fair and reasonable profit. The disposition of these appeals is to be governed by the ASPR non-weighted profit guidelines, not by the Merchant Marine Act or other statutes or regulations reflecting different policy considerations. As indicated above, a consideration pervading all of the non-weighted guidelines is the basic policy of the Department of Defense, to procure supplies and services from responsible sources at fair and reasonable prices calculated to result in the lowest overall cost to the Government. If considerations of cost to the Government had been determinative, NObs-3556 would have

been awarded to Bath. In awarding this contract to appellant, the Government put aside considerations of cost in order to keep the Quincy yard in operation. Viewed from this standpoint, the award of NObs-3556 to appellant constituted a form of extraordinary financial assistance.

Appellant's reliance upon the circumstances leading to the award of NObs-3760, 3761, and 3762 lacks significant merit. The prices proposed by the various shipyards for the DD 945-51 were not far apart if compared with the relatively wide disparity between the prices proposed by Bath and appellant for the DD 936-8. Moreover, as stated previously, it is apparent that appellant did not submit the lowest proposal if the cost of plan work is taken into account. In any event we find that the award of NObs-3760, 3761 and 3762 on the basis of the Navy's allocation policy did not involve a financial sacrifice for the benefit of a contractor approaching the magnitude of that involved in the award of NObs-3556.

In the case of the award of NObs-3648, we are unable to find that the Government made the kind of financial sacrifice which it made in the award of NObs-3556. Having made the award of NObs-3556 to appellant the Government was no longer confronted with a clear-cut choice between allowing the Quincy yard to shut down, or awarding appellant a contract at a price greatly in excess of the lowest proposed price. Indeed, appellant's proposal was the only proposal solicited. The Government would have us compare the per ship price under NObs-3648 with the per ship price submitted by Bath for the DD 936-8. However, Bath was awarded NObs-3615 at about the same time as appellant was awarded Nobs-3648. NObs-3615 involved

three vessels in addition to the three vessels Bath was already constructing under NObs-3371. There is no evidence as to what price Bath might have proposed had the Navy solicited from it a proposal for construction of the DD 943-4, an additional two ships to be delivered at about the same time as the three ships required under NObs-3615. 4/ Moreover the $16,250,000 award price per ship under NObs-3648 was only $27,000 higher than the price established in NObs-3760, awarded to Bath eighteen months after the award of NObs-3615; and was about $200,000 per vessel less than the price established in NObs-3762, awarded to Puget Sound.

From the record presented we are unable to find that the award price of NObs-3648 included a bonus to appellant measured by the difference between the per ship price under NObs-3648 and the per ship price offered in the Bath DD 936-8 proposal. The record does not establish that the Government might have saved money by awarding this contract to another shipyard. NObs-3648 was awarded to appellant solely on the basis of the Navy's allocation policy. In our opinion the allocation of NObs-3648 to appellant did not, in itself, amount to extraordinary financial assistance within the meaning of Factor (d).

CONCLUSIONS UNDER FACTOR (d)

Consistent with the above quoted statement of the Court of Claims as to the effect

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4/ The delivery schedules under NObs-3615 and NObs-3648 were as follows:

	NObs-3615	NObs-3648
First Vessel	1 April 1957	June 1957
Second Vessel	1 August 1957	October 1957
Third Vessel	1 December 1957	

of Government financial assistance in determining allowable profit, we conclude that through the award of NObs-3556 appellant received extraordinary financial assistance within the meaning of Factor (d). Factor (d) thus tends to depress the additional profit, if any, to which appellant might be entitled under NObs-3556 through application of other guidelines. We further conclude that appellant did not receive extraordinary Government assistance under NObs-3648. Factor (d) thus has no effect on the additional profit, if any, to which appellant might otherwise be entitled under NObs-3648.

Factor (e) - Extent of the Contractor's Investment. This factor is stated as follows:

> "The extent of a contractor's total investment (i.e., both equity and borrowed capital) in the performance of the contract will be taken into consideration in determining the amount of the fee or profit."

Comparison with Newport News Investment.

In Newport News Shipbuilding and Dry Dock Co. v. United States, supra, the Court of Claims indicated that if the Board were to find that capital was small in relation to profit actually earned, Factor (e) might operate adversely to the contractor. In our decision on the reinstated Newport News appeal we made specific quantitative findings as to the contractor's assets (e.g. land acreage, plant square footage, total equity and borrowed capital). We further found that except for certain ship repair facilities, Newport News used all of its facilities in varying degrees for construction of the RANGER.

In the present appeals we lack evidence to support findings as specific as those which we made in Newport News. The Bethlehem Shipbuilding Division was only one of several corporate divisions. The Shipbuilding Division alone included eleven different shipyards in 1954. Because of its corporate structure appellant was unable to determine the equity and borrowed capital actually invested in the Quincy yard. (Tr. 1-95) However we find from the evidence presented that the acquisition cost of Quincy facilities capitalized under Bethlehem's depreciation policies totaled approximately $11,322,000 in 1954. This total did not include land, railroad properties, portable tools and small equipment. (Exh. A-6) The cost of replacing the Quincy yard facilities in 1954 exceeded $50,000,000. (Tr. 3-30, 3-35) We further find that to some degree all of the Bethlehem-owned facilities at the Quincy yard were used to build the five destroyers, although, for lack of other work, these facilities were used at very low capacity. (Tr. 1-81) Furthermore, as contrasted with Bath, which subcontracted for most of its design work, appellant's Central Technical Department, financed out of corporate funds, was available to perform design work as necessary in connection with construction of the destroyers. (Tr. 5-13, 5-55)

In our decision in the reinstated Newport News appeal we found that as of 31 December 1954, Newport News' investment in total operations, expressed as both equity and borrowed capital, totaled $67,700,000. As indicated above we are unable to derive a comparable figure with respect to appellant's total investment in the operations of the Quincy yard. However, it is fair to state that as of

the award of NObs-3556 and 3648, most, if not all, of the capital invested in the Quincy yard was committed to the performance of those contracts. This capital included facilities valued for replacement purposes in excess of $50,000,000. As in Newport News we are unable to find that capital was so small in relation to return as to be an indicator of the possible generation of excessive profit.

Effect of Denial of Escalation.

In considering the impact of Factor (e) on the disposition of these appeals, appellant would have us contrast the Navy's protracted refusal to pay appellant's escalation claim with the relatively prompt payments of escalation claims under NObs-3371, 3760, 3761 and 3762. Appellant maintains that as contrasted with other yards, appellant has been required to finance the costs of inflation over a prolonged period of time, thus committing additional working capital to the performance of NObs-3556 and 3648.

In making this argument appellant assumes a result in these appeals favorable to it. The possibility of a protracted dispute arising out of the escalation clause has been considered above under Factor (b). Furthermore none of the other yards were paid escalation until delivery of the required vessels was accomplished, although the guaranty period might not have expired. (Exh. A-14, A-18, A-20) All of the contractors for DD 931 class vessels were on an equal footing insofar as they had to finance the costs of inflation during actual construction of the vessels. In our opinion the Navy's

refusal to pay appellant's escalation claim is not relevant to the application of Factor (e).

Had appellant not received the usual progress payments, which was not the case here, its investment in relation to return would have been substantially increased. We do take into account in applying Factor (d) the difference noted above between the reserve withheld under appellant's contracts and the comparable reserve withheld under other contracts for DD 931 class vessels. However this difference is insignificant when viewed in the context of all of the considerations relevant to the application of Factor (e).

CONCLUSIONS UNDER FACTOR (e)

As indicated above we are unable to find that appellant's investment was so small in relation to return as to have a depressing effect on the profit allowable under other guidelines. We are also unable to find that appellant's investment was so large in relation to its return as to support a profit allowance greater than that considered allowable under other guidelines. We thus consider Factor (e) to be neutral as it affects the disposition of these appeals.

Factor (f) - Character of Contractor's Business. This factor is stated as follows:

> "Recognition must be given to the type of business normally carried on by the contractor, the complexity of manufacturing techniques, the rate of capital turnover, and the effect of each individual procurement upon such

business. For example, where a contractor is engaged in an industry where the turnover of working capital is low, generally the profit objective on individual contracts is higher than in those industries where the turnover is more rapid."

The Shipbuilding Industry.

Under this factor we are considering characteristics of the American shipbuilding industry as a whole at the time of award of the contracts involved in these appeals. With respect to the shipbuilding industry at that time, we stated the following in our decision on the reinstated Newport News appeal:

"One of the distinguishing features of new ocean vessel construction contracts, and a characteristic particularly true of vessel construction by appellant [Newport News], is that the contracts normally are long-term, requiring up to 5 years for completion of the vessel and sometimes an added period for financial settlement. The end product is large and complex, requires a proportionate investment in facilities, and the maintenance of a large technical and engineering staff and a work force of skilled people who are difficult to replace, tending to produce large and inflexible overhead costs which can create greater losses in periods of low activity than in some other types of business. When the Government is the customer under a fixed price contract, payment is normally slower than payment by a private customer under a fixed price

> contract. The low turnover of invested capital and the other circumstances described increase the demand for working capital. This was true of the RANGER contract." (71-1 BCA at p. 40,447)

Evidence in the record now before us supports identical findings, with insignificant variations. We accordingly consider the above quoted statement from Newport News as applicable to the disposition of these appeals.

Value Added.

In Newport News we further found that "the end product, RANGER, obviously reflected the addition of very substantial value to the acquisition value of material prior to its incorporation in the vessel." (71-1 BCA at p. 40,447) The following table provides a comparison between appellant's material costs and labor costs in constructing the five destroyers:

TABLE VII

	Material Cost	Labor Cost
DD 936-8	$23,558,600	$14,898,200
DD 943-4	15,917,400	8,712,100
Total	$39,476,000	$23,610,300

(ASBCA No. 10316, Rule 4, Tab 4)

This comparison does not reflect the further contribution made by appellant's facilities and overhead personnel to the value added to purchased materials. We accordingly

find, as we did in Newport News, that in constructing the five destroyers appellant added very substantial value to the acquisition value of purchased material incorporated into the vessels.

Appellant's Facilities and Personnel.

In 1954 the Quincy yard was among the three major shipyards in the United States, the two others being Newport News and New York Shipbuilding Co. The Quincy yard was large, covering 150 acres and included complete shops and facilities. Unlike other yards, Quincy manufactured the propulsion machinery for ships it built. During World War II the Quincy yard was engaged in a shipbuilding program at least as difficult and diverse as that undertaken by any other yard. (Tr. 1 -12-15, Exh. A-8) As mentioned previously, appellant's Central Technical Department, a large ship design organization, was located at Quincy. Apprentice schools and training programs were located at Quincy. (Tr. 1-16) Between 1943 and 1953 total employment at Quincy was almost three times that at Bath (ASBCA No. 10316, Rule 4, Tab 6). We find that for the purposes of considering the application of Factor (f) appellant's facilities and personnel compared favorably with those of Newport News.

CONCLUSIONS UNDER FACTOR (f)

In Newport News Shipbuilding and Dry Dock Co. v. United States, supra, the Court of Claims stated the following in considering Factor (f):

". . . The rate of capital turnover is the ratio of invested capital to

> sales. When a large and costly plant is necessarily required to produce a given volume of sales, the ratio of profit to sales would be larger than it should be if a small and cheap plant sufficed for the same volume. Similarly, if the 'value added' is relatively high that is, the completed product has a high value in relation to the value of the materials purchased, the ratio of profit to sales should be greater and in the converse situation, less. There is nothing to show how the Board applied this factor to the case at hand."

It is readily apparent from the above findings, viewed in the light of the Court's statement, that as a shipbuilder appellant's rate of capital turnover was low and that the effect of individual procurements upon appellant's business was great, particularly in periods of depressed activity which was the case in 1953-4. We have found that the value added by appellant to purchased materials was substantial. Furthermore, it is obvious from our discussion under Factor (c) that highly complex production techniques were involved in the construction of the destroyers. We conclude that Factor (f) tends to support an allowance to appellant of greater profits under NObs-3556 and NObs-3648.

Factor (g) - Contractor's Performance. This factor is stated as follows:

> "In addition to the factors set forth in 3-101, the contractor's past and present performance should be evaluated in such areas as quality of product, quality control, scrap

> and spoilage, efficiency in cost control (including need for and reasonableness of cost incurred), meeting delivery schedules, timely compliance with contractual provisions, creative ability in product development (giving consideration to commercial potential of product), engineering (including inventive, design simplification, and development contributions), management of subcontract programs, management of Government property, and any unusual services furnished by the contractor, where a contractor has consistently achieved excellent results in the foregoing areas in comparison with other contractors in similar circumstances, such performance merits a proportionately greater opportunity for profit or fee. Conversely, a poor record in this regard should be reflected in determing what constitutes a fair and reasonable profit or fee." 5/

Factor (g) is to be applied prospectively. Newport News Shipbuilding and Dry Dock Co. v. United States, supra. Thus we are called upon to evaluate various aspects of appellant's performance under NObs-3556 and NObs-3648. Also relevant is appellant's performance under Navy contracts, and its overall competence as a shipbuilder, prior to the award of NObs-3556.

5/ ASPR 3-101, relating to price negotiations, does not add any additional considerations relevant to the disposition of these appeals.

Quality of Vessels Delivered Under NObs-3556 and NObs-3648.

Most of the evidence under this heading involves a comparison between the DD 931 class destroyers delivered by appellant and those delivered by Bath. Mr. Miller testified that the principal measure of ship quality is the number of defects discovered during the course of acceptance trials and, later, during periods of post fitting-out and post shakedown availability. (Tr. 5 - 155-6) The evidence establishes, and we find, that the Navy considered that the DD 931 class vessels delivered by appellant and Bath were all of very good quality. (Tr. 5-10)

However, in at least two significant instances, vessels delivered by Bath were defective, whereas the vessels delivered by Bath under NObs-3371 included Westinghouse turbines. During acceptance trials the turbine rotors cracked when operated at the intended revolutions per minute (rpm). The Navy accepted the ships which had to be operated at reduced rpm pending redesign of the rotors to eliminate the cracking problem. Because of this deficiency the contract price of NObs-3371 was reduced by $30,000. (Exh. A-13) Appellant's turbines, manufactured by General Electric Company, did not experience the cracking problem. (Tr. 5-22-5) The problem with the Westinghouse turbines was attributed to defective manufacture on the part of Westinghouse. (Tr. 5-26)

Prior to the award of contracts for DD 931 class vessels, Bath had constructed the DL 2 and 3, and appellant had constructed the DL 4 and 5. All four vessels

included Westinghouse turbines which experienced similar rotor cracking problems. Appellant's decision to procure General Electric turbines resulted from its previous experience with the Westinghouse turbines. Appellant decided that the quality of the Westinghouse turbines was deteriorating from an engineering standpoint. (Tr. 6-65) The record does not disclose the reason for Bath's decision to install Westinghouse turbines in the DD 931, 932 and 933.

Bath later encountered difficulties in connection with the forced draft blowers installed in the DD 945-7. The forced draft blower was an integral part of the boiler combustion system. At the time the DD 931 program commenced, Westinghouse was the sole source for such blowers. The Navy then decided to develop alternative sources for what was viewed as an essential and expensive piece of machinery. (Exh. A-16) After appropriate testing, blowers developed by Carrier Corporation and Hardy-Tynes were placed on the Qualified Products List, meaning that they met the Navy specifications for blowers. (Tr. 5-15-16)

Due to a protracted strike at Westinghouse, Bath decided to procure blowers from Carrier Corporation for installation in the DD 945-7. When the DD 945 was taken on builder's trials, in April 1958, it was found that the Carrier Corporation blowers would not operate in parallel, resulting in failure of the vessel to achieve its full power requirements. The Navy informed Bath that it would not accept the DD 945-7 due to the blower problems. Bath

decided to order replacement blowers from Westinghouse, but then found that it could not cancel its contract with Carrier Corporation unless it were willing to incur substantial cancellation charges. The Navy then agreed to accept the DD 945 for limited service, with the understanding that the guaranty period would be extended indefinitely until satisfactory blowers were installed. Carrier then produced modified blowers, which performed as intended. (Exh. A-16; Tr. 5 - 17, 18)

The reports describing the results of preliminary acceptance trials of the DD 936-8 and 943-4 indicate a few defects, but none which appear to have affected the overall operational capability of the vessels (ASBCA No. 10316, Rule 4, Tab 4).

Appellant contends that the turbine cracking problems encountered under NObs-3371, and the forced draft blower problems encountered under NObs-3760, reflect adversely on Bath's performance as compared with appellant's performance under NObs-3556 and 3648. The Government acknowledges that it held Bath contractually responsible for correction of the defects, but contends that since the defects were attributable to the malfunctioning of vendor components which had been certified on the Navy's Qualified Products List for use by shipbuilders, the defects should not be taken into account in evaluating Bath's performance. The Government further argues that since many pieces of equipment on a ship malfunction at the time of delivery, isolated defects such as these are not relevant to evaluating comparative performance for the purpose of applying Factor (g).

We agree with the Government that the defects in the Bath ships relied upon by appellant should be considered in context for the purpose of applying Factor (g). However, the difficulties experienced by Bath in connection with the turbines and forced draft blowers were significant, and we find that as compared with the vessels delivered by appellant, they detracted from the overall quality of the Bath vessels. In the case of the forced draft blower problems, arising under NObs-3615, we agree with the Government, in view of the strike at Westinghouse, that Bath acted reasonably in procuring the Carrier Corporation equipment, which apparently had not been adequately tested prior to its inclusion on the Navy's Qualified Products List. Accordingly we do not consider, for purposes of applying Factor (g), that the forced draft blower problems reflect adversely on Bath's performance as a shipbuilder. But in the case of the turbine difficulties, we have found above that appellant, on the basis of its prior experience in constructing DL's, changed its source of supply. Bath, on the other hand, in performing under NObs-3371, elected not to do so for reasons unexplained by the record. Accordingly, we are unable to find that Bath was entirely without blame for the failure of the DD 931-3 to operate at full capacity when delivered.

Compliance with Delivery Schedule.

The following table compares delivery dates with actual delivery dates:

TABLE VIII

DD No.	Contract DAtes	Actual Dates
936	15 December 1956	30 November 1956
937	15 February 1957	28 February 1957
938	15 April 1957	10 July 1957
943	June 1957	20 November 1957
944	October 1957	26 February 1958

The record does not include information sufficient for us to prepare a table comparing the timeliness of appellant's deliveries with that of other contractors. The record also does not establish to what extent, if any, the differences between contract delivery dates and actual delivery dates were attributable to changes. Moreover, the record does not reveal any complaints on the part of the Navy regarding the periods of several months each between the contract delivery dates and actual delivery dates of the DD 938, 943 and 944. In the case of the DD 938 Mr. Markowich testified that a three-month delay did not detract from overall delivery timeliness for this type of vessel. From the evidence presented we find that appellant's deliveries under NObs-3556 were timely. However, in the absence of an explanation as to excusable circumstances, we find that the five-month delay in delivering the DD 943 and the four-month delay in delivering the DD 944 reflect adversely, to a minor degree, on appellant's performance under NObs-3648.

Engineering Improvements.

As indicated above, appellant had constructed the DL 4 and 5 prior to the award of NObs-3556. Partly on the basis of its DL experience, appellant, in April 1954, suggested to the Navy certain

engineering improvements in the DD 931 class vessels which were not reflected in the Navy specifications. Appellant suggested use of a boiler which incorporated features that resulted in an appreciable weight saving without increasing required maintenance. Appellant further suggested a complete redesign of the reduction gears for the DD 936 which would reduce the risk of overloading. These two recommendations were not solicited by the Navy. On the basis of a study performed by appellant for the Bureau of Ships, appellant also recommended an improved steam cycle involving modifications to the boiler plant. In appellant's view adoption of these three recommendations would increase the reliability and cruising radius of the destroyers. (Tr. 1-59, 2-128-33) There is no evidence that Bath made similar suggestions, although it too had relevant prior experience in constructing DL destroyers.

The two unsolicited recommendations pertaining to the modified boilder and redesign of the reduction gears were adopted by the Navy for use in constructing all DD 931 class destroyers except for the DD 931-3. (Tr. 2-134) In the Navy's view, adoption of those recommendations led to a better ship. (Exh. A-24) The suggested improvements to the steam cycle were not adopted by the Navy for use in constructing the five destroyers required under NObs-3556 and 3648, but were adopted in connection with the construction of later DD 931 class vessels. (Tr. 2-134) The three engineering improvements suggested by appellant were not regarded as breakthroughs in the state of the art, but reflected the kind of engineering contribution that can only be made by a shipyard having an alert and

capable design and engineering organization such as appellant or Newport News. (Tr. 2 - 136-7)

The Government contends that since the engineering recommendations made by appellant were not state-of-the-art breakthroughs, they do not entitle appellant to any special consideration under Factor (g). According to the Government appellant's suggestions are best characterized as improvements on an earlier class of ship that can normally be expected from a shipyard. However, these improvements were viewed by the Navy as meritorious, and the record does not indicate that any other contractor for DD 931 class vessels, including Bath, made equally significant recommendations. Factor (g) does not limit engineering or product improvement contributions to state-of-the-art breakthroughs. Accordingly we find that appellant's engineering contributions have a positive effect on an evaluation of appellant's performance.

Cost.

The total costs of constructing DD 931 class vessels, broken down by contract, are stated on Table VI, supra. In order to facilitate a comparison between the costs incurred by the four shipyards to whom contracts were awarded, the costs of construction per ship are set forth in the following table:

TABLE IX

Contract	No. of Ships	Contractor	Per Ship Cost
NObs-3371	3	Bath	$14,648,104
NObs-3556	3	Bethlehem	17,734,867
NObs-3615	3	Bath	14,271,590
NObs-3648	2	Bethlehem	16,514,350
NObs-3760	3	Bath	14,578,684
NObs-3761	2	Ingalls	17,326,819
NObs-3762	2	Puget Sound	15,888,855

During construction of its five vessels appellant imposed rigid controls on material, labor and overhead in an effort to reduce costs as much as possible. (Tr. 1-63) Nevertheless, as indicated by Table IX, appellant's cost per ship was higher than that incurred by any other yard excempt Ingalls, which incurred greater costs under NObs-3761 than did appellant under NObs-3648. As indicated previously the principal differences between appellant's costs and Bath's costs was the large disparity in overhead costs. A comparison between appellant's and Bath's proposals for the DD 936-8 indicates an estimated overhead difference of about $2,300,000 per ship. (Exh. A-1) Even when the Quincy workload was higher, at the time proposals for the DD 931-3 were submitted, appellant's per ship overhead was estimated at about $1,400,000 higher than Bath's overhead. (Exh. G-5)

Mr. Mack-Forlist testified that in the shipbuilding industry it is generally understood that the efficiency of a shipyard is measured in terms of output per manhour, not in relation to dollar cost. (Tr. 4-19, 4 - 81-3) Such a comparison would exclude overhead costs as a measure

of yard efficiency. However, even if relative efficiency is evaluated solely as a function of manhours, the evidence presented does not support a favorable comparison between appellant and Bath. In performing under NObs-3371, Bath expended approximately 5,320,000 manhours, compared with an original bid estimate of 6,337,600 manhours. (Exh. A-14a) In performing under NObs-3556 appellant expended 5,589,570 manhours not including 406,050 hours for drafting and 78,780 hours expended by appellant's Central Technical Department. In performing under NObs-3648, appellant expended 3,347,974 labor hours not including drafting and Central Technical Department hours. (ASBCA No. 10316, Rule 4, Tab 4) When it submitted its proposals, appellant had estimated 5,709,000 labor hours for construction of the DD 936-8 and 3,524,000 for construction of the DD 943-4. A comparison between appellant and Bath on the basis of actual manhours per ship is shown as follows:

TABLE X

Contract No.	DD No.	Average Labor Hours Per Ship
NObs-3371	931-3	1,773,333
NObs-3556	936-8	1,863,190
NObs-3648	943-4	1,673,987

It is apparent that in performing under NObs-3648 appellant realized the "learning curve' benefits of its experience under NObs-3556. The record does not disclose the actual labor hours expended by Bath in performing under NObs-3615, concerning which learning curve benefits would be similarly expected. Bath's proposal for the DD 936-8, on the basis of which NObs-3615 was awarded,

included a comparatively high labor hour estimate of 1,990,400 per ship. (Exh. A-1) In denying escalation under NObs-3615 the Navy considered that in preparing its proposal for the DD 936-8, Bath should have considered its manhour experience under NObs-3371, which indicated that its labor hours would be less than the total indicated in its proposal. (Exh. G-13)

In discussing labor costs we further note that appellant's proposals for the DD 936-8 and 943-4 included average hourly wage rates of $2.41 and $2.42 respectively, as compared with Bath's hourly wage rate under NObs-3615 of $2.00. (Exh. A-1) The difference was attributed principally to the respective geographic locations of the contractors, i.e. prevailing wage rates were generally higher in Quincy, Massachusetts than in Bath, Maine.

Prior Performance.

Under Factor (g) appellant's performance as a shipbuilder prior to award of NObs-3556 is an appropriate topic of consideration. In our decision on the reinstated Newport News appeal, we considered under this heading the World War II performance of Newport News. Between 1942-4, the Quincy yard delivered 86 vessels including 1 battleship, 4 aircraft carriers, 5 heavy cruisers and 6 destroyers. During the same period Newport News delivered 39 vessels including 1 battleship, 7 aircraft carriers, and 6 light cruisers. (Exh. A-8) With respect to Essex class carriers, built by both Quincy and Newport News, Quincy's performance slightly exceeded that of Newport News on the critical

criterion of delivery time. (Tr. 3-43) Appellant's World War II ships were considered to be of high quality. Like Newport News, appellant received a letter of appreciation from the Secretary of the Navy, then Mr. Forrestal, dated 1 September 1945, the day of the surrender of the Empire of Japan. In the letter Mr. Forrestal stated that "Among the companies which gave our fleet the power to attack, yours has been preeminent." (Exh. A-9) From the evidence presented we find that appellant's World War II performance compared favorably with that of Newport News as to number and diversity of ships constructed, quality of the ships, and delivery time. The evidence is insufficient for us to make findings as to comparative costs of constructing World War II vessels.

Future Performance.

Appellant presented evidence as to its performance in constructing vessels subsequent to construction of the DD 936-8 and 943-4. We consider such evidence as irrelevant to our determinations under Factor (g).

CONCLUSIONS UNDER FACTOR (g)

When appellant's performance is measured in accordance with the criteria set forth in Factor (g), it is apparent that except for cost, appellant's performance equalled or exceeded that of other yards. We so conclude, on the basis of findings made under the above headings derived from the text of Factor (g). On the element of relative cost, it is clear that appellant's costs far exceeded those incurred by Bath, and to a lesser degree exceeded those incurred by Puget Sound. Only Ingalls, which suffered a loss on

NObs-3761 prior to escalation, incurred costs approximating the magnitude of appellant's costs.

Since Factor (g) speaks of "efficiency in cost control" we have considered whether appellant's strenuous efforts to keep labor and material costs to a minimum should weigh more heavily in applying Factor (g) than its incurrence of the high overhead which was the principal cause of the wide cost disparity between appellant and Bath. However, we do not regard Factor (g) as precluding consideration of the cost impact of maintenance by appellant of uneconomical overhead facilities and personnel during a period of declining business. The Court of Claims was apparently in accord with this view when it stated in Bethlehem Steel Corporation v. United States, supra (at p. 153) that "We think the Board would be within its charter in denying a return on that part of the overhead which exceeded the allocation of other shipbuilders." We do not overlook the contributions to appellant's overhead costs made by the maintenance of facilities under the facilities contract, and by appellant's Central Technical Department which the Navy desired to keep in operation through the award of NObs-3556. But the record does not indicate the extent to which these activities contributed to appellant's entire overhead.

As indicated above appellant would have us evaluate its cost efficiency solely on the basis of labor hours expended. Such an evaluation would exclude from consideration other elements of cost which make up the contract price, or the total cost to the Government. By ignoring such costs we

would not be adhering to the basic policy consideration underlying all of the guidelines, that supplies, and services shall be procured from responsible sources calculated to yield the lowest overall cost to the Government.

On the basis of the foregoing discussion we conclude that the relatively high total cost incurred by appellant in performing under NObs-3556 and NObs-3648 has a depressing effect on otherwise allowable profit. However this depressing effect is substantially offset by appellant's superior performance as a shipbuilder prior to the award of NObs-3556 and 3648, its delivery of good quality vessels under those contracts, and the engineering improvements which it made. As between NObs-3556 and NObs-3648 we make two noteworthy distinctions. Under NObs-3648 appellant incurred costs approximating $1,200,000 per ship less than its costs per ship under NObs-3556. Thus the depressing effect of excessive cost on allowable profit under NObs-3648 is less than the comparable effect under NObs-3556. The comparatively favorable result under NObs-3648 is counteracted in minor measure by the delays in delivery of the DD 943 and 944 noted previously.

Factor (h) - Subcontracting. This factor is stated as follows:

> "(1) In negotiating the profit or fee, subcontracting as a factor shall be segregated for separate evaluation, particularly as it bears on the contractor's technical supervision and management responsibility, financial investment, and degree of risk, as outlined above. The degree and nature

of subcontract programs vary on a broad spectrum. While it is not possible to define the exact profit or fee treatment to be accorded each situation, the general guidelines which follow shall be taken into consideration.

"(2) The evaluation of a contractor's subcontracting program should not consist merely of applying arbitrary percentages of profit to subcontract prices in negotiating the prime contract price. A relatively large amount of subcontracting by itself need not result in negotiation of correspondingly lesser profit or fee--the character and circumstances of the subcontracting and the effect on the prime contractor's costs must be taken into account. Although purchased material and subcontracting work are usually properly included in the base upon which profit or fee is computed, instances may arise in which a significant portion or portions of a contract are subcontracted in such a way that only a minimum amount of responsibility or risk remains with the prime contractor. In such case, in order to prevent unreasonable pyramiding of profit or fee, the amount of profit or fee attributable to the subcontracted work should be substantially less than where the contractor uses his own resources and retains substantial responsibility or risk. Of primary importance is the degree to which the subcontracting provides a better product and lower costs, with timely delivery, and in which the contractor assumes heavy managerial and technical effort, responsibility and

risk. Particular attention should be given to the contractor's managerial and technical effort, responsibility and risk with respect to subcontracts under major weapon system contracts where a substantial portion of total contract cost is attributable to subcontracting of major components. Consideration must be given to the relationship which the prime contractor's estimated profit or fee on subcontracted work bears to his cost of placing and managing such subcontracted work.

"(3) In establishing a contractor's fee or profit, favorable consideration shall be given to:

(i) the company's policies and procedures which energetically support Government small business and labor surplus area programs;

(ii) any unusual efforts which the contractor displays in subcontracting with small business and labor surplus area concerns, particularly for developmental type work likely to result in later production opportunities; and

(iii) effectiveness of the company in subcontracting with and furnishing assistance to such concerns, as compared to other comparable contractors.

In this connection, it is the responsibility of the purchasing activity to

examine the contractor's past and present effectiveness and plans for seeking out qualified small business and labor surplus area concerns, and to require the contractor during negotiations to document his past, present, and planned performance in these areas."

Extent of Subcontracting.

According to the internal Navy business clearance document prepared in support of the award of NObs-3556, appellant informed the Navy that in constructing the DD 936-8 it would place subcontracts and purchase orders aggregating approximately $16,300,000, but that there would be no subcontracts in excess of $300,000. (Exh. A-2) In its proposal for the DD 943-4 appellant stated that it would place subcontracts and purchase orders aggregating at least $10,900,000. (Stipulation Exhibit F) We find that about one-third of the cost incurred by appellant in constructing the five destroyers represented amounts paid to subcontractors and suppliers.

At the hearing in the reinstated appeals Mr. Strohmeier testified that in the shipbuilding industry, a significant distinction is drawn between a subcontract and a purchase order. He stated that a purchase order generally includes supply items procured from vendors outside the shipyard, while a subcontract calls for work performed within the shipyard by another company using its own work force. (Tr. 1 - 55-6) He made a "wild guess" that about one percent of the material cost involved material suppliers actually performing work at the Quincy

yard. (Tr. 3-88) There is no evidence supporting a more reliable figure.

CONCLUSIONS UNDER FACTOR (h)

In the absence of contradictory evidence we find that Mr. Strohmeier's distinction between a subcontract and a purchase order, as those terms are used in the shipbuilding industry, is valid. The distinction is important since, under Factor (h) the critical consideration is the extent of managerial and technical effort, responsibility and risk retained by the prime contractor on the one hand, or delegated to subcontractors on the other. If appellant's subcontracting, within Mr. Strohmeier's definition of that term, were substantial, we might find that appellant delegated a significant portion of its effort, responsibility and risk. We would also have to consider the responsibility for managing the subcontracted work retained by appellant. However from the evidence presented we are unable to find that appellant delegated to subcontractors a substantial portion of the overall effort, responsibility and risk under NObs-3556 and 3648. We conclude, as we did in the reinstated Newport News appeal, that Factor (h) is without influence on the disposition of the present appeals.

Factor (i) - Unrealistic Estimates.

This factor is stated as follows:

"If records reveal that a contractor's actual costs are consistently lower than his estimated costs (indicating a practice of excessive estimates), and if the contractor

refuses to provide what seems to be a reasonable estimate of costs, a lower profit or fee should be considered."

Appellant's Estimates.

There is no evidence that during World War II or the years immediately preceding the award of NObs-3556 and 3648 appellant consistently estimated its costs to be considerably in excess of its actual cost experience. With respect to NObs-3556 and 3648, we are also unable to find an excessive disparity between the total estimated costs stated in appellant's proposal and its actual construction costs. Indeed appellant's labor hour estimates proved to be quite accurate. For the five destroyers appellant estimated a total of 9,233,000 hours. (Exh. A-1) Appellant actually expended a total of 9,484,036 hours (Exh. A-29). The higher number of hours expended is attributable in large part to the performance of change orders.

The Government contends that appellant's overhead estimates were excessively high. However, as found above, appellant's proposals for the DD 936-8 and 943-4 were prepared on the assumption that its work under the two destroyer contracts would be burdened with virtually all of appellant's fixed overhead. Appellant had no reason to believe that substantial additional business would materialize during performance of these two contracts, affording appellant a broader overhead distribution base. We are accordingly unable to find that appellant estimated the overhead allocable to construction of the DD 936-8 and 943-4 at unreasonably high levels.

CONCLUSIONS UNDER FACTOR (i)

On the basis of the above findings we conclude that Factor (i) does not have a depressing effect on the profit which would otherwise be allowed appellant.

DECISION

In Newport News Shipbuilding and Dry Dock Company v. United States, supra, the Court of Claims stated (at p. 121) that:

> ". . . we recognize that it is never possible to fix a single exact line where and only where the profits are reasonable. It is a band, not a line, involving an exercise of judgment which can claim accuracy only within broad limits. . . ."

The Court stated further that if the profit actually accrued was within the band, no action was called for. The Board was to allow escalation under Article 6,

> ". . . only if it found a material and substantial difference between the actual profit and what it determined to be reasonable."

However, consistent with paragraph 3-808.1 of the non-weighted guidelines, the Court indicated (at p. 120) that comparisons between profit levels should be made in dollars, not percentages. Nothing in the Court's decision in Bethlehem Steel Corporation v. United States, supra, indicates a change in the Court's views on these matters.

Consistent with a statement made by the Board in its decision on the reinstated

Newport News appeal, appellant contends that the Government has the burden of proving that appellant is not entitled to the escalation which would otherwise be allowed under the applicable Article 6 formulas. According to appellant the Government has not carried that burden. In Newport News we stated that the Government has an initial burden, but the benefit of such burden to the contractor is not entirely clear when application of the guidelines is said to be controlling.

In our opinion the matter of overall burden of proof with respect to the appeals now before us has become academic. The basic issue is what profits should appellant be allowed respectively under NObs-3556 and NObs-3648. As required by the Court of Claims we have made specific findings and conclusions concerning application of each of the non-weighted guidelines. These findings and conclusions govern the disposition of these appeals.

As stated previously, Factor (a) is of no assistance to appellant, since the award of both contracts resulted from considerations other than procurement of the vessels from the responsible source offering the lowest price on the basis of competition. Thus appellant's entitlement to additional profit, if any, must be based upon the application of other guidelines. In order to provide boundaries for consideration of what might constitute a range of reasonable profit to appellant under Factors (b) through (i), we have developed the following table (see Table XI next page) which shows comparative dollar profits per ship after escalation, under the DD 931 class contracts, in relation to comparative contract prices. The record does not indicate that the value of

change orders or differences in the scope of work were so divergent among the various contracts as to warrant consideration of change orders or scope of work differences for the purpose of the relatively gross comparisons which we make here.

In view of the several distinctions which have been made in our findings between the application of the guidelines to allowable profit under NObs-3556 on the one hand, and under NObs-3648 on the other, we deal separately with each of the two contracts.

NObs-3556 (ASBCA No. 10316)

The Government contends that the profit previously allowed by the Board falls within the range of fair and reasonable profit, and therefore should not be increased. The Government relies heavily on what it characterizes as the "subsidized" nature of the award. As found above in our discussion under Factor (d) the award of NObs-3556 to appellant at a price considerably in excess of that proposed by the lowest responsible offeror amounted to extraordinary Government assistance, which has a depressing effect on allowable profit. If Factor (d) alone governed the disposition of this appeal we would agree with the result sought by the Government since the allowance of additional profit would be tantamount to a further return on the extraordinary assistance. Factor (d) alone indeed would justify a profit allowance even less than that previously allowed by the Board.

However, as indicated by Table XI, appellant's per ship profit under NObs-3556 is, as of the Board's original deci-

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sion, only slightly greater than one-third the average per ship profits earned by Bath under NObs-3371, 3615 and 3760. Under NObs-3371 and 3760 the Navy allowed escalation sufficient for Bath to earn profits of about 2,230,000 per ship. With full escalation appellant's profit would still fall about $627,000 lower per ship than that of Bath.

Contract No.	Contractor	Contract Price Per Vessel	Dollar Profit Per Ship After Escalation	Dollar Profit Per Ship With Escalation Allowed In Part
NObs-3371	Bath	$15,425,000	$2,230,206	
NObs-3556	Bethlehem-Quincy	17,674,000	1,647,693 *	$886,743 **
NObs-3615	Bath	15,492,320	2,357,667 ***	
NObs-3648	Bethlehem-Quincy	16,250,000	1,590,204 *	889,718 **
NObs-3760	Bath	16,223,000	2,234,103	
NObs-3761	Ingalls	16,225,000	376,516	
NObs-3762	Puget Sound	16,445,000	1,607,795	

* Profit if appeals are sustained in full
** Profit with escalation allowed by Board's original decision
*** Escalation denied

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Our findings with respect to risk under Factor (b), with respect to the nature of the work to be performed under Factor (c), and with respect to the character of the contractor's business under Factor (f) tend to support a considerable reduction in the dollar disparity between the profit allowed appellant and the profit allowed Bath. In particular, as indicated in our decision on the reinstated Newport News appeal, a contractor is entitled to be rewarded under the guidelines for assuming greater than the usual risks, as appellant did under NObs-3556.

The only other factor which we considered to have some impact on allowable profit was Factor (g), under which we evaluated several aspects of appellant's performance. Our findings under that factor were mixed. On the one hand we found that appellant's incurrence of high costs has a depressing effect on allowable profit. On the other hand we found that appellant's delivery of high quality vessels, its recommendations for engineering improvements which were adopted by the Navy, and its superior performance as a shipbuilder in World War II, tended to support an allowance of additional profit. The depressing effect on profit of appellant's high overhead, which was the principal cause of the price and cost disparaties between appellant and Bath, has already been taken account of in the application of Factor (d). Consistent with our findings under Factor (g), and in accordance with the policy objective of rewarding superior performance through higher profits, we consider that the application of Factor (g) counteracts in some measure the unfavorable result obtained under Factor (d).

As indicated by the above discussion the guidelines which control the disposition of ASBCA No. 10316 are Factors (b), (c), (d), (f), and (g). The other factors were considered to have no effect, either upward or downward, on allowable profit. In our opinion the profit previously allowed by the Board under NObs-3556 was below the range of fair and reasonable profit when the controlling guidelines are applied collectively. In our view a fair and reasonable profit to appellant under NObs-3556 would approximate half the profit recovered by Bath under NObs-3371 and 3760, under which escalation was allowed. The average profit allowed Bath under those contracts amounted to $2,232,155 per vessel. Accordingly we determine that appellant is entitled, under NObs-3556, to additional escalation sufficient to enable it to earn a profit of $1,116,023 per vessel. The arithmetical consequences of this result on appellant's total escalation claim will be indicated below.

NObs-3648 (ASBCA No. 10317)

In our findings under Factor (d) we were unable to characterize the award of NObs-3648 as extraordinary Government assistance. As indicated by Table XI, supra, the per vessel price under NObs-3648 compares favorably with the prices established in NObs-3760, 3761 and 3762, and we did not consider as valid the Government's comparison between the respective prices in NObs-3648 and NObs-3615. Our findings under Factor (d), as applied to NObs-3648, have a critical effect on allowable profit. The significant depressing effect of Factor (d) on allowable profit under NObs-3556 is not carried over to a consideration of

allowable profit under NObs-3648.

Appellant's per vessel profit under NObs-3648, as of the Board's original decision, again is only slightly greater than one-third the per ship profits recovered by Bath under NObs-3371, 3615 and 3760. As further indicated by Table XI, appellant's per ship profit under NObs-3648 is now about half the per ship profit earned by Puget Sound under NObs-3762, in which the per vessel price was higher than the comparable price in NObs-3648.

Factors (b), (c) and (f) again tend to support the allowance of additional profit to appellant, although Factor (b) argues less strongly in appellant's favor than it did for the purpose of determining allowable profit under NObs-3556. We also found some distinctions under Factor (g), the performance guideline, namely that the depressing effect of excessive cost was less, but that delays in delivery should be taken into account. However, appellant is again entitled to be rewarded for its prior performace as a shipbuilder, its delivery of high quality vessels and its engineering improvements.

With full escalation appellant's profit under NObs-3648 would still fall short of Bath's average profit under its three contracts by about $684,000 per vessel. Appellant's profit would be quite close to the profit recovered by Puget Sound under NObs-3762, under which full escalation was allowed. Our findings under Factors (b), (c) and (f) tend to support a profit allowance to appellant at least as great as that recovered by Puget Sound. Puget Sound's costs were about $650,000

per vessel less than appellant's costs under NObs-3648, and the depressing effect of appellant's excessively high overhead must be taken into account pursuant to Factor (g). We also take into account appellant's relatively late deliveries under NObs-3648. These adverse consequences arising from application of Factor (g) are counteracted in substantial measure by appellant's performance in other areas.

If appellant were seeking a profit approaching the profits recovered by Bath, we would have doubts as to its allowability since the costs incurred by appellant exceeded those incurred by Bath by about $2,000,000 per vessel. However, the difference in costs between appellant, under NObs-3556 and Puget Sound under NObs-3762 was not nearly so great. The significance of appellant's relatively high cost is further reduced when it is recognized that Puget Sound was allowed full escalation, and a 1.6 million dollar profit under NObs-3762, although its costs per vessel exceeded those of Bath by about 1.3 million dollars on the average.

On the basis of the relevant guidelines, applied collectively, we conclude that the profit recovered by appellant under the Board's previous decision was below the range of fair and reasonable profit. In determining what constitutes a fair and reasonable profit under NObs-3648 we have considered the higher costs experienced by appellant relative to those experienced by Bath and Puget Sound. However, in view of the inapplicability of Factor (d), and our discussion of relative cost in the context of Factor (g), such considerations of cost can have at most

only a minimal depressing effect on the profit otherwise considered fair and reasonable. As indicated previously, appellant's delivery delays also have at most, only a minor depressing effect. The record does not indicate a substantial disparity in cost to the Government of ships delivered under NObs-3648, as compared with those delivered under NObs-3760, 3761 and 3762. Appellant is seeking a profit under NObs-3648 approximating $640,000 less than the profit recovered by Bath under NObs-3760, a contract under which the risk with respect to lead yard plans was less than the risk assumed by appellant under NObs-3648, By application of the guidelines we determine that appellant is entitled to recover the profit obtained by full escalation.

SUMMARY

On the basis of the foregoing, ASBCA No. 10316, as reinstated pursuant to the decision of the Court of Claims, is sustained to the extent that appellant is entitled under NObs-3556 to recover additional escalation in the amount of $687,840 computed in the following manner:

Total profit per vessel allowed by this decision	$1,116,023
Less: Profit per vessel previously allowed by Board	886,743
Additional escalation allowed per vessel	229,280
Number of vessels	X 3
Total additional escalation allowed	$ 687,840

The appeal is denied as to the remainder of appellant's $2,282,849 escalation claim under NObs-3556.

ASBCA No. 10317, as reinstated pursuant to the decision of the Court of Claims, is sustained in its entirety. Accordingly, appellant is entitled to recover the entire $1,528,872 additional escalation claimed.

Of the $3,911,821 total additional escalation claimed in the two appeals, appellant is entitled to recover $2,216,812.

Dated 11 December 1972.

Daniel M. Arons
DANIEL M. ARONS
Member of Division No. 10
Armed Services Board of
Contract Appeals

I Concur

I Concur

Ruth C. Burg
RUTH C. BURG
Member of Division No. 10
Armed Services Board of
Contract Appeals

Thomas E. Burns
THOMAS E. BURNS
Member of Division No. 10
Armed Services Board of
Contract Appeals

(Signatures continued)

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I Concur I Concur

Harris J. Andrews, Jr.
HARRIS J. ANDREWS, Jr., Vice Chairman, Armed Services Board of Contract Appeals and Member of Division No. 10

Richard C. Solibakke
RICHARD C. SOLIBAKKE, Chairman Armed Services Board of Contract Appeals and Member of Division No. 10

I certify that the foregoing is a true copy of the decision and opinion of the Armed Services Board of Contract Appeals in ASBCA Nos. 10316 and 10317 (Reinstated), appeals of Bethlehem Steel Corporation, rendered in conformance with the Board's Charter.

Dated: 22 January 1973

George L. Hawkes
GEORGE L. HAWKES, Recorder Armed Services Board of Contract Appeals

BETHLEHEM STEEL CORPORATION

v.

The UNITED STATES

No. 44-68.

United States Court of Claims

Feb. 19, 1975.

George Vradenburg, III, New York City, for plaintiff. Albert R. Connelly, New York City, attorney of record.

Howard G. Slavit, with whom was Asst. Atty. Gen. Carla A. Hills, for defendant. Steven J. Bercik, Washington, D.C., of counsel.

Before DURFEE, Senior Judge, and DAVIS, SKELTON, NICHOLS, KASHIWA, KUNZIG and BENNETT, Judges.

NICHOLS, Judge:

This case of Wunderlich Act review of a contract dispute under Dispute Clause procedure (41 U.S.C. § 321-322) is now before us for the third time. On the first occasion, 423 F.2d 300, 191 Ct. Cl. 141 (1970), we held that the Armed Services Board of Contract Appeals (ASBCA) had erred as a matter of law in not following certain Armed Services Procurement Regulations (ASPR) we considered applicable to the dispute. After Board preliminary proceedings reported at 71-1 BCA ¶ 8640, Bethlehem on May 10, 1971, applied to us for an order terminating stay and for other relief. This we denied in an unreported order, without opinion. The Board proceedings then resumed and resulted in the decision now under review, 73-1 BCA ¶ 9898. We affirm.

Our 1970 opinion details the controversy as it had evolved up to that time and we need not repeat it all here. Briefly, Bethlehem had built five Navy destroyers under two fixed price contracts. NObs-3556 and 3648, both of which contained clauses allowing for labor and material escalation, but enabling the Contracting Officer to deny any upward adjustment thereunder in whole or in part, if he found that it was not required to enable the Contractor to earn a fair and reasonable profit under the contract, Art. 6, Par. (e). After full performance, plaintiff claimed $3,347,000 escalation

under NObs-3556 and $2,404,900 under NObs-3648. The latter claim has now been allowed by the Board in its entirety and having been dismissed is not before us for review. The original Board decision allowed $1,064,151 under NObs-3556 making a total profit of 5% of costs. The Board's theory was that plaintiff had agreed to a limit of 5%. We were unable to find evidence of agreement to that limit. Further, the Board had determined the level of reasonable profit without reference to the published guidelines of the Department of Defense which told how contract clauses limiting contractors to reasonable profit levels (hereinafter, profit limitation provision) were to be interpreted and applied.

In Newport News Shipbuilding & Dry Dock Co. v. United States, 374 F.2d 516, 179 Ct. Cl. 97 (1967), we had already held that in making a profit limitation decision under a Navy contract clause of the same type, the Board had erred in not following published guidelines. On retrial, the Board, as we indicated it should, followed the guidelines enacted after the contract date and before its original decision, hereinafter called the "unweighted guidelines." It allowed Newport News full escalation, 71-1 BCA ¶ 8705. The case was settled on that basis. In Bethlehem , the fact appeared that the Department of Defense had superseded the original "unweighted guidelines" with so-called "weighted guidelines", after the original Board decision in Newport News and before that in Bethlehem.

Plaintiff in Bethlehem argued

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for use of the "weighted guidelines" on retrial. Defendant seemed to argue for no guidelines at all, attacking the "weighted guidelines" as unsuitable for the Bethlehem contract even if required for most others. This was because, in defendant's view, the "weighted guidelines" would fail to allow weight for the fact the Navy had awarded this contract to Bethlehem, though it was a high bidder, to keep its Quincy, Massachusetts facility in the shipbuilding business. At that point, however, defendant indicated no preference for the "unweighted guidelines".

This issue caused us much concern. Since, in Newport News we had held a guideline regulation to apply to a contract written at an earlier date, when no guidelines existed, it seemed consistent that any further amending or superseding provisions should be applicable likewise, right up to the original Board trial on the facts. This would make the amended or "weighted guidelines" the proper ones to use in the Bethlehem retrial. What happens, however, if the guidelines are amended or modified again, between the original trial and retrial of the issue? In Newport News, apparently by mutual consent, the new guidelines were not given effect at the retrial and the Board used the ones it should have used at the original trial. It was nevertheless obvious to us that this was not the only possible answer.

The determination of a supposedly reasonable level of profit by administrative fiat after the event, and not by operation of the market place, is not an easy operation that anyone can perform. Without guidelines the power to do it confers, as we said in Bethlehem I, a

kind of roving absolutism inimical to our institutions (423 F.2d p. 308, 191 Ct. Cl. p. 155). In the administration of our most widely used system of profit limitation under Government contracts, the Renegotiation Act of 1951, 50 U.S.C. (App.) § 1191 and ff., and its predecesors back to 1942, the need for guidelines has been recognized from the beginning, almost, and they are provided both in statutory provisions and in regulations. 50 U.S.C. (App.) § 1213(e); 32 C.F.R. § 1460.1 and ff. The ASPR indicated a recognition of the same need, and we were understandably reluctant to believe there could be any profit limitation provisions in Department of Defense contracts, they were not intended to apply to. By the same token, new regulations, we would presume, reflected more extended experience with profit limitation, and would if applied to previously existing contracts, produce a more satisfactory result than previous regulations or no regulations at all. On the other hand, it certainly was possible the authors of regulations might be unaware at times of all the previously awarded contracts remaining unsettled, to which they might apply, and they might obtain unforeseen and undesired results. If this occurred, they should be free to correct their errors.

As we have recently held in Hills Transp. Co. v. United States, 492 F.2d 1394, 204 Ct. Cl. 51 (1974) whether, in the absence of express provision, a procurement regulation can have retroactive application to a contract earlier awarded, is not to be decided by any wooden rules, but by reference to the character and intent of the contract and of the regulation involved. Here, factors favoring retroactive application are the long

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lapse of time under these shipbuilding contracts, between original award and final settlement, and the remedial effect of a guideline regulation, any regulation, as against the assignment of a "roving absolutism" to a Contracting Officer in granting or denying escalation.

In view of the foregoing considerations we deemed it unwise to nail defendant inescapably to the mast of the "weighted guidelines" method. While stating that as things were, plaintiff was entitled to use of that method on retrial, we held that even then, defendant could make a retroactive change in the method. Our words, as reported, were as follows:

* * * * * *

> As we have said, we see no injustice or anomaly in applying profit limitation techniques, as the Pentagon may have amended and prescribed them from time to time, up to the date of the determination. We would presume that changes were intended to clarify and simplify, as well as to reduce the subjective factors in the mind of the administering official. To some extent amendments may reflect earlier departures in actual practice, to a large extent no doubt they are the product of experience. If anything has been slipped in which would impair vested rights unless limited to prospective application only, let it be pointed out. If we have erred in thinking the "weighted guidelines method" is feasible to apply to the instant contracts, the Pentagon even now could amend or supplement its regulation, and the Board would be bound, provided no impairment of

> vested rights was attempted. Any amendment purporting to reaffirm the position now claimed, that officials determining a reasonable level of profit under clauses such as Article 6(e) are not subject to any published guidelines whatever in certain cases, at least would advisedly be made in light of the recent statement of the Supreme Court: "* * * a broad, roving authority, a type of administrative absolutism [is] not congenial to our law-making traditions." Gutknecht v. United States, 396 U.S. 295, 306, 90 S. Ct. 506, 24 L.Ed.2d 532 (1970). [423 F.2d at 307, 191 Ct. Cl. at 154-55.]

It was express that the change should, if made, be in the regulations, and therefore by the rule-making arm of the Secretary of Defense, not his adjudicatory arm, the ASBCA. A change in the rules by the latter would be nothing but a reversion to the "do it yourself guidelines" and "seat of the pants navigation" we condemned in the Newport News decision and again in this. Members of the ASBCA are required to be "learned in the law" and can hardly be also expected to be so expert as not to need guidance as to the techniques of reasonable profit determination. If the rule-making body was to change the rules, it was implicit that body should follow its customary formalities in making rules, and receive the advice from within and without the Government that it normally would. Both the "unweighted guidelines" and the "weighted guidelines" afford internal evidence that the needed expertise exists within or is available to the Department of Defense. A third implicit requirement was that the purported "rule" should really have general application and not be just an attempt to influence a lawsuit. We referred to "The

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Pentagon" meaning that all bodies in or about that vast structure might perform in the roles appropriate to them under the organization of the Department.

What actually happened was put before us in Bethlehem's 1971 motion. It is assumed for purposes of this opinion that our denial of the motion did not establish a "law of the case" barring consideration now. The ground was unstated and it could have been on several grounds.

Shortly after our decision came down the Navy legal member put before the ASPR Committee, the rule-making committee having supervision over the ASPR, a request for a "deviation". Quoting parts of our decision, he advanced the Navy's position that the "weighted guidelines" were not intended to apply to contracts awarded, as Bethlehem's was, before 1963. The Committee decided, as recorded in its minutes, that mandatory retroactive application of the weighted guidelines was not intended, and particularly with respect to escalation clauses. Deviation was not required. The Committee also agreed application of the weighted guidelines was not feasible and they were intended only for negotiation of future contracts. A deviation was approved to the extent others might think the guidelines applied. In taking this action, the Committee recognized it would leave the unweighted guidelines in ASPR 3-808 for application. They were not considered as effecting a substantive change in the contract. The Navy member had listed ten contracts with unsettled escalation claims under similar clauses, to which the "deviation" would apply. This included the two

Bethlehem contracts here involved. The Navy's reason for asserting unfeasibility appears to have been primarily that the "weighted guidelines" effectuated an objective that obtained in 1963 to attract more contractors to defense work. This need did not exist in 1954 when the Bethlehem contracts were awarded and the object was then to place contracts at the lowest possible prices.

The ASBCA subsequently held, correctly it would appear, that under ASPR 1-109.3, the Committee had authority to approve a "deviation" of this kind, provided it was unanimous, and a major policy was not involved. Both these conditions were satisfied. See also DOD Instru. 5126.3, December 20, 1961; Government Contract Reports § 825. It could have published a regulation or directive, without higher level approval, subject to those conditions.

The ASBCA considered it was bound by this "deviation" to apply the unweighted and not the weighted guidelines. It correctly read our decision as holding that it was not the proper body to make this kind of decision, and that one properly made elsewhere would bind it.

The Board, after trial, applying the non-weighted guidelines, awarded plaintiff full escalation under Nobs-3648, but only $687,840 additional escalation over the previous decision under Nobs-3556 being 6.3% of cost. The sum of $2,282,849 would have been required for full escalation, and the Board denied the excess of this figure over $687,840.

Plaintiff does not attack the

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Board's techniques in applying the unweighted guidelines, or rather its attack does not focus upon any variation between those techniques and one or more identified parts of the non-weighted guidelines themselves. In general, the Board appears to make a conscientious and reasoned effort to apply them fairly. Plaintiff says it has a "vested" right to the "weighted guidelines" and under them would recover full escalation as a mathematical certainty. We are not so sure as to that but defer to the Pentagon's experts who, as plaintiff notes, themselves believe such guidelines would produce substantially higher results, at least.

If defendantwanted to use the unweighted guidelines, it is regrettable it did not so inform us in 1970. To have disposed of all Art. 6(e) escalation claims by a uniform method would have had advantages apparent to any mind, and the method was already in use for Newport News. Any benefit from future advances in profit control technique could have been sacrificed in the circumstances. Nor did defendant tell us then that the weighted guidelines were purposely inflated to attract more bidders. We also deplore the failure to inform Bethlehem of the contemplated change in the rules. There are certain amenities normally to be expected in the conduct of litigation. To obtain ex parte a change in the ground rules and present them to the adjudicating tribunal as fait accompli and binding on it, will not impress the ordinary mind as entirely cricket. However, our problem is whether to react only to clear cut and demonstrated illegality, or whether to allow our sense of undirected outrage to prolong this already inordinately prolonged litigation, to the advantage of no one

knows whom. In the case of the Government, we realize that the right hand often does not know what the left hand does. Actions are taken that are, in the aggregate, outrageous, yet may be quite innocent in the minds of the individual actors.

We cannot make our own determination of a reasonable profit level in view of our holding in Newport News that the issue is factual, and our obligation to leave factual issues to Board determination despite previous errors, unless the Board procedure is inadequate and unavailable. United States v. Anthony Grace & Sons, 384 U.S. 424, 86 S. Ct. 1539, 16 L.Ed.2d 662 (1966). The slow progress of this case does not seem imputable to the Board so much as to the novelty of the issues and the complexity of the case. If the job of determining a reasonable profit level has to be done all over again, it is the Board that must do it.

The "unweighted guidelines" used here were considered and approved by us in the Newport News case supra. No contention is made that these guidelines are not fair and reasonable, of themselves. In plaintiff's eyes, they are just not as productive of a high level of reasonable profit as the preferred set. As a matter of fact the "unweighted guidelines" bear a strong family resemblance to the Congressionally enacted set in the Renegotiation Act, cit. supra. In adjudicating Bethlehem I, we formed the impression the Department of Defense had abandoned them as unsatisfactory, but this is now shown to have been erroneous. The "weighted guidelines" were put in effect for wholly different reasons, as has appeared above.

Plaintiff's serious legal attack on

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the Board decision has three main heads: (1) the alleged ex parte approach by the Navy member to the ASPR Committee, (2) that Bethlehem has a vested right in use of the "weighted guidelines" method, and (3) that it was "feasible" to use those guidelines.

1. As a matter of law, this court has often regarded ex parte approaches as invalidating adjudicatory actions. Camero v. United States, 375 F.2d 777, 179 Ct. Cl. 520 (1967). Jarett v. United States, 451 F.2d 623, 195 Ct. Cl. 320 (1971). However, it has not attempted to apply the same standards to rule making. Everyone knows that an ex parte approach may lie behind many a statute. When we indicated therefore, that a change in the rules must originate in a rule making body, we indicated that such a change might be effected by the procedures normal to such bodies. Plaintiff has not cited a statute or regulation applicable to the ASPR Committee, invalidating an ex parte approach by one of its members. We wonder if an approach to an organized body by one of its own members can ever be deemed ex parte in the pejorative sense of the word.

2. Plaintiff slso says it had a vested right in the use of the "weighted guidelines" procedure. This echoes a provision in our former opinion, quoted above, intimating that in changing its regulation, the defendant could not impair vested rights. Where does the alleged vested right of the plaintiff originate? Not in the contract, wherein plaintiff did not bargain for use of any method of determining a reasonable level of profit in case Art. 6(e) had to be administered. Not in the regulation itself, since our

reading of it makes it inherently subject to change, unless the change impairs vested rights of other origin. Not in our former decision. We are not empowered to create vested rights against the Government except in the form of money judgments. Such rights might come into being as res judicata, collateral estoppel, or "law of the case", but we see none of these here. There has been no final judgment to give rise to the first two, and as to law of the case, it works against plaintiff if at all, insofar as our "law of the case" stated in Bethlehem I was purposely hedged, and plaintiff's contention just comes back to depend on plaintiff's interpretation of that decision, which we reject.

The irreparable flaw in plaintiff's claim to a vested right in the "weighted guidelines" is that in 1954 plaintiff deliberately made contract Nobs-3556, including Art. 6(e). If Art. 6(e) subsequently came up for implementation, the most plaintiff could demand was determination of its acceptable profit level by some fair and reasonable method, of general applicability, and not one freshly invented for its particular case. This has now been accorded to it.

3. Plaintiff also says it would be "feasible" to apply the "weighted guidelines" echoing our language that these guidelines might be changed if it were not "feasible" to use them. Plaintiff also says use of these guidelines leads inexorably to allowance of its entire escalation claim without deduction. The Board in response quotes dictionary definitions of "feasible" as "possible" or "practicable" or "capable of being done", and other definitions as what is "suitable" or "reasonable". It con-

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cludes, correctly, that we intended the broader meaning. The paragraph taken as a whole, indicates that a general change in the regulations made for any legitimate reason is acceptable. "Unfeasibility" of the prior regulation is merely an example. We regret having used such an ambiguous terminology. In the area of profit limitation the subjective cannot be avoided entirely. If a technique of determining a reasonable level of profit produces a result that shocks the sense of fairness or justice, use of it is not "feasible", and should be avoided.

The Board also points out, correctly, that the major premise of Bethlehem I decision was our objection to decision of profit limitation issues under Art. 6(e) of the involved contracts, by the use of do-it-yourself or seat-of-the-pants guidelines. A minor premise was the belief, right or wrong, that the regulations provided proper published guidelines for all cases, and the conclusion, that such published guidelines should be followed. As the Board points out, use of the "unweighted guidelines" per rule adopted under the ASPR constitution, implements, rather than violates, every significant part of our decision. Had we known they wanted to use the "unweighted guidelines" we would probably have expressed our approval. We may have thought matters would be handled differently than they were, in some respects, but we did not frame a mandate to demand all that we expected. Indeed, to describe out opinion as a mandate at all is an exaggeration. In 1970 we did not have the power to tell the Board what to do, that we now have under 28 U.S.C. § 1491, as amended by Pub.L. 92-415. The Board suspended the case to allow plaintiff

to apply to this court when it declared its dissatisfaction with the guidelines to be followed. It did more than the law required of it, to ascertain our wishes and apply them. Our so-called mandate was in reality, and was intended, more as a summary of the legal options open to defendant on the legal options open to defendant on the retrial of the case.

In view of the foregoing, the Board decision under review is not contrary to substantial evidence, is not contrary to law, and is not arbitrary or capricious. By Wunderlich Act standards, it must therefore be affirmed.

Plaintiff's motion for summary judgment is denied. Defendant's cross motion for summary judgment is allowed. Judgment is entered for plaintiff in the amount determined by the Board, which was for Contract Nobs-3556, $1,064,151 under the original decision and $687,840 additional under the decision now under review, or a total of $1,751,991, with adjustment for any portion of the said sum already paid.

BENNETT, Judge (dissenting):

During the year 1954, plaintiff was awarded two contracts, Nobs-3556 and Nobs-3648, for the construction of three destroyers and two destroyers, respectively. Plaintiff was not the low bidder for the Nobs-3556 contract, but was awarded the contract nevertheless in pursuance of the Government's policy of continuing the existence of an essential defense facility. Plaintiff was the only shipbuilder asked to submit a proposal for Nobs-3648, and, on the same policy ground, was awarded that contract as well.

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Both contracts contained provisions requiring the contractor to exclude from its cost estimates any contingency allowances intended to offset anticipated increases in labor and material costs during the period of construction. In return, the Government promised to reimburse the contractor, according to an agreed formula, for any increases in labor and material costs which ultimately occurred during that period, except as limited by the following article 6(e) of the contracts:

> (e) The Contracting Officer may deny, in whole or in part, any upward adjustment in the contract price required under this Article if the Contracting Officer finds that such adjustment is not required, in whole or in part, to enable the Contractor to earn a fair and reasonable profit under this contract.

When plaintiff entered into the contracts at issue, there were no published guidelines for determining "fair and reasonable profit" in a given case. Sometime prior to August 1963 the Department of Defense published "unweighted" guidelines, and in August 1963 those unweighted guidelines were superseded by the "weighted" guidelines method of determining reasonable profits. 32 C.F.R. §§ 3.808-1 et seq. (1965).

When plaintiff's contracts were completed (the last of the five destroyers was delivered on February 26, 1958), plaintiff sought from the contracting officer labor and material escalation costs of $3,347,500 on Nobs-3556 and $2,404,900 on Nobs-3648. In neither case was the amount of the escalation costs in dispute, but

the contracting officer refused to permit recovery of any of those costs on the basis that such adjustment was unnecessary "to enable the Contractor to earn a fair and reasonable profit." Article 6(e), supra. If the decision of the contracting officer had stood, plaintiff's profit on the two contracts would have been 3 percent and 2.3 percent of cost, respectively; the full escalation sought by plaintiff, on the other hand, would result in profit margins of 9.3 percent and 9.6 percent.

Plaintiff's appeal to the ASBCA from the contracting officer's decision was partially successful, the board awarding plaintiff that portion of escalation costs which brought its profit margin on both contracts to 5 percent of cost. Though the weighted guidelines were in effect at the time of the board's decision, the board did not use them or refer to them.

Plaintiff appealed to this court from the ASBCA decision. The result was the court's opinion in Bethlehem Steel Corp. v. United States, 423 F.2d 300, 191 Ct. Cl. 141 (1970), which is hereafter referred to as Bethlehem I. In that opinion the court recalled that in an earlier case with very similar facts,[1] it had applied the existing Department of Defense regulations which set out unweighted guidelines for determining a

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1. Newport News Shipbuilding & Dry Dock Co. v. United States, 374 F.2d 516, 179 Ct. Cl. 97 (1967).

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reasonable profit margin to a contract entered into prior to the effective date of those regulations. It followed that in Bethlehem I plaintiff was also entitled to application of the existing regulations, i.e., the weighted guidelines, and the court so held (with a reservation to be discussed, infra):

> * * * Plaintiff desires to take its chances under the "Weighted guidelines method" and it has a legal right to do so. [423 F.2d at 307, 191 Ct. Cl. at 154.]

Indeed, even defendant in Bethlehem I accepted the general principle that the weighted guidelines should apply to contracts entered into prior to the regulation's effective date:

> * * * Defendant does not now deny that it [the regulation setting out the weighted guidelines] would govern most decisions limiting or refusing otherwise justified labor and material escalation under Article 6(e), and there is nothing in it [the regulation] that suggests an intent to narrow the former scope. * * * * [423 F.2d at 305, 191 Ct. Cl. at 150.]

Defendant argued in Bethlehem I however, that plaintiff should be an exception to the rule because plaintiff had been awarded the shipbuilding contracts in spite of the fact that other contractors could have built the ships at lower cost, and in order that plaintiff would not close down its facilities. In rejecting this argument, the court noted, first, that the desired exception was not to be

found in the regulation and had "every earmark of having originated in the active mind of defense counsel."[2] The court also rejected defendant's assertion that the parties had agreed to a profit level of 5 percent in consideration of plaintiff's being awarded the contract, and that the weighted guidelines would result in a higher unintended level of profits:

> * * * The alleged agreement to a 5% level, in a contract that viewed prospectively could have resulted in anything from a loss to a windfall profit level, according to its terms, must be regarded as located in defendant's counsel's eyes alone. [423 F.2d at 306, 191 Ct. Cl. at 152.]

After its determination that plaintiff had a "legal right" to application of the weighted guidelines, however, the court added the following comments:

> As we have said, we see no injustice or anomaly in applying profit limitation techniques, as the Pentagon may have amended and prescribed them from time to time, up to the date of the determination. We would presume that changes were intended to clarify and simplify, as well as to reduce the impact of subjective factors in the mind of the administering official. To some extent amendments may reflect earlier departures in actual practice, to a large extent no doubt they are the product of experience. If anything has been slipped in which would impair vested rights unless limited to prospective application

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2. 423 F.2d at 305, 191 Ct. Cl. at 151.

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> only, let it be pointed out. If we have erred in thinking the "Weighted guidelines method" is feasible to apply to the instant contracts, the Pentagon even now could amend or supplement its regulation, and the Board would be bound, provided no impairment of vested rights was attempted. * * [423 F.2d at 307, 191 Ct. Cl. at 154.]

Seizing upon the above comments, which the majority now identifies as an option open to defendant on retrial of the case, the Navy promptly requested from the ASPR committee a "deviation" from the use of weighted guidelines with respect to plaintiff's contracts and eight other shipbuilding contracts. The ASPR committee granted the deviation, stating that application of the weighted guidelines to contracts entered into prior to the effective date of the regulation is not feasible, since the weighted guidelines effect a substantive change in the standards existing at the time the contracts were entered into and were intended for the development of a profit objective for negotiation of future contracts. In lieu of the weighted guidelines, the ASPR committee prescribed application of the superseded unweighted guidelines to plaintiff's contracts.

Defendant was successful in convincing the ASBCA to follow the ASPR committee's "deviation" and thus to apply the unweighted guidelines. In doing so, the ASBCA ruled that plaintiff was entitled to full escalation on the Nobs-3648 contract, but only partial escalation (to a 6.3 percent profit margin) on the Nobs-3556 contract. Plaintiff is convinced, and defendant's actions seems to confirm

the fact, that if the ASBCA had used the weighted guidelines rather than the unweighted guidelines, plaintiff would have recovered virtually all of the escalation under the Nobs-3556 contract. Plaintiff thus requests that this court reaffirm its statement in Bethlehem I that plaintiff has a "legal right" to application of the weighted guidelines.

The issue presented for decision here is easily stated. Has defendant shown that the weighted guidelines method is not "feasible" to apply to the contract at issue? If not, then plaintiff has a legal right to its application. It is my belief that the weighted guidelines are entirely feasible to apply and that plaintiff should receive the benefit of their application. I would remand to the board for that purpose.

The term "feasible" has, of course, more than one meaning. As Judge Nichols indicates, it can mean "possible" or "reasonable" or "suitable." There can be no dispute that it is possible to apply the weighted guidelines to plaintiff's contracts. In fact, both plaintiff and defendant are able to anticipate what the approximate result of such an application would be. Furthermore, it would not be "unreasonable" to apply those guidelines in the sense that their use would result in an unusual or absurd result, or as Judge Nichols states, one that "shocks the sense of fairness or justice." Rather, it appears that if they were used appropriately in the manner demonstrated in some detail by the court in Bethlehem I, the result would be an indicated profit margin for plaintiff of between 9 percent and 12 percent. The maximum profit

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plaintiff can receive from escalation here is 9.3 percent, in any event.[4]

Defendant has suggested three reasons why the use of weighted guidelines is "unsuitable," if we are to use this as the definition of the word "feasible." I will deal with them in turn.

First, defendant states that it is desirable that all shipbuilding contractors whose contracts contained article 6(e) should have the reasonableness of their profits determined by the same method--namely, unweighted guidelines. But there is no inherent reason why this should be so. We were aware in Bethlehem I that the unweighted guidelines had in all likelihood been applied in the Newport News, supra, contract, and others. We nevertheless stated that plaintiff was entitled to the benefit of the existing regulation specifying weighted guidelines. It was presumed that the weighted guidelines represented an improvement over the earlier method, particularly because they reduced the "impact of subjective factors in the mind of the administering official."[5] Moreover, defendant's interest in consistency was not apparent in Bethlehem I wherein defendant argued that no guidelines should be applied to determine the reasonableness of plaintiff's profits. It seems that defendant desires consistency of

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4. Other shipbuilding contractors received escalation, even though such escalation brought profit levels to 15.2 percent, 15.32 percent, and 10.1 percent in three instances.

5. 423 F.2d at 307, 191 Ct.Cl. at 154.

treatment only when it sees some advantage to itself arising therefrom.

The second of defendant's arguments with respect to feasibility is that the greater profits which plaintiff would receive upon application of the weighted guidelines were not contemplated when the contract was entered into. The short answer to this contention is that the court expressly rejected it in Bethlehem I; the court stated that there was no agreement respecting profit, and that the contract could have resulted in anything from a loss to a windfall profit level, as both parties realized.

The third and final of the defendant's arguments is a reiteration of the ASPR committee's stated reason for granting the deviation. That reason, as has been stated above, was that retroactive application "is not feasible, since it [the weighted guidelines] effected a substantive change in the standards existing at the time the contracts were entered into and were intended for the development of a profit objective for negotiation of future contracts." Looking first to the alleged frustration of "intention," it is noteworthy that there is no evidence in the record to support the ASPR committee's statement that only prospective application was intended. As the court noted in Bethlehem I, the regulation contains no such limitation and there is no reason to infer one. In addition, defendant did not argue in Bethlehem I for prospective application only, but agreed rather that the regulation would generally cover contracts such as the one in question. Even the "Notes and Filing Instructions" which accompanied the

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regulation and which were cited by the ASPR committee state:

> The revised paragraph 3-808 is authorized for immediate use and maximum practical use is encouraged. However, to allow for an initial training period in the use of the weighted guidelines method, mandatory use is not required until after 1 January 1964. Mandatory use is prescribed for all applicable procurements initiated after 1 January 1964.

Defendant argues further, though, that the fact that the weighted guidelines had the potential for higher profits in order to attract the "best possible industrial capabilities" proves that only prospective application was intended. The conclusion does not follow from the premise, however. First, it should be noted that the court in Bethlehem I was aware that the regulation had the potential for greater profits. The regulation itself, section 3.808-1(a), stated that use of weighted guidelines "will result in a wider range of profits which, in many cases, will be significantly higher than previous norms." The regulation also stated that effective national defense requires attraction of the "best industrial capabilities" and that such capabilities would be dissuaded by "low profit opportunities." Thus, the ASPR committee said nothing which the court had not already read in the regulation itself. Secondly, though the emphasis on potentially higher profits may have been directed to attracting future business, this does not prove that prior contracts were to be excluded from coverage, in the absence of a statement

to that effect which could easily have been written into the regulation. The court was aware at the time of Bethlehem I that the guidelines, whether weighted or unweighted, were used primarily in negotiating the price to be paid a contractor on a future contract. Determining reasonable profits after completion of contract performance is an unusual situation. Nevertheless, in both Newport News, supra, and Bethlehem I, the court found that absent language in the regulation to the contrary, the existing guidelines were to apply. Indeed, there is no reason why the guidelines cannot be applied. The "Notes and Filing Instructions" accompanying the weighted guidelines include the statement: "This method if a rational, uniform, and equitable approach for evaluating the factors which must be considered in determining a proper profit or fee objective." What is rational, uniform, and equitable for others is equally so for plaintiff.

The ASPR committee's statment that the weighted guidelines represent a substantive rather than a procedural change contradicts the entire basis for decision in Bethlehem I and must be dismissed. The new regulation does not guarantee higher profits, but represents simply a less subjective method of determining fair and reasonable profit. That the less subjective procedure has the potential for higher profit computations only confirms the known fact that changes in procedure can have an effect on substance.

To summarize thus far, I have demonstrated that there is no valid reason why the weighted guidelines cannot feasibly be applied to plaintiff's contract.

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Indeed, neither the ASPR committee nor counsel in this case has brought anything to the court's attention which the court was unaware of at the time it stated that plaintiff had a legal right to the application of weighted guidelines, or which could have had a bearing on the court's decision. Defendant is in reality still clinging to its assertion, rejected in Bethlehem I that the parties did not contemplate that plaintiff would recover more than a 5 percent profit.

The majority opinion states that the court's opinion in Bethlehem I was less a "mandate" than a "summary of the legal options open to defendant." If this be so and surely it is not, then Bethlehem I was no more than an advisory opinion--something which this article III court has no authority to give. In reality, Bethlehem I mandated that the weighted guidelines be used, but protected its flank by suggesting that if, for reasons unknown to the court, the application of weighted guidelines would lead to an unfair or absurd result, "the Pentagon" could amend or supplement the regulation to prevent such a result. The court did not give "the Pentagon" carte blanche to evade the mandate on any pretext, or, as Judge Nichols states to "attempt to influence a lawsuit." Yet the Pentagon attempted to do just that.

This case bears a certain similarity to Pacific Far East Line, Inc. v. United States, 394 F.2d 990, 184 Ct.Cl. 169 (1968). In that case MARAD adopted new criteria for determining the amount of profits which the Government could recapture from a subsidized ship operator. MARAD had originally indicated that the new criteria would be retroactively applied to Pacific Far East Line's earlier years of operation, but when it

realized that this would benefit PFEL in the sum of $750,000, it withdrew retroactive application. The court would not permit such a reversal by MARAD for the following reason:

> * * * We are left with the bald circumstance that MARAD changed its method of accounting after it discovered that PFEL was entitled to a large sum under its original procedure. MARAD's only concern must have been to secure for the defendant the maximum amount of money in the form of recapture. As such, this situation takes on the appearance of market place haggling and unreasonable retroactivity which offended this court in American President Lines, Ltd. v. United States, 154 Ct.Cl. 695, 705, 291 F.2d 931, 936 (1961). * * *. [184 Ct.Cl. at 189, 394 F.2d at 1001.]

In the same way, defendant in this case has reversed itself with regard to the use of weighted guidelines after realizing that plaintiff stands to recover greater profits from their use. Defendant's evasion of the Bethlehem I decision in order to influence the results in this lawsuit should not be permitted. Defendant has failed to show weighted guidelines are not feasible here or would produce unfair or absurd results. The majority opinion upholding defendant's change of rules in the middle of the game impairs plaintiff's vested rights against "roving administrative absolutism." The majority condemns as not "cricket" and as "deplorable" and as "outrageous" what has happened here but tolerates it. This is because the issue of a reasonable profit

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is said to be factual and for administrative determination according to guidelines which are fair and reasonable and of general application although subject to change at any time for any legitimate reason. My conclusion is that even as stated the test does not fit the facts before us in such a way as to support the majority's result in the case.

I have dealt above with the first of two main arguments plaintiff makes in this case, namely, that the weighted guidelines should have been applied because infeasibility thereof has not been demonstrated, particularly because this court in Bethlehem I was aware of the factors relied upon by defendant as allegedly showing infeasibility. However, plaintiff has a second cogent argument. Plaintiff says that the board acted arbitarily and capriciously in applying unweighted guidelines. The majority opinion passes offf without elaboration or refutation the second argument which plaintiff develops at length. Plaintiff makes a good case against the board's implementation of the unweighted guidelines. On either or both grounds plaintiff should prevail, and defendant should lose this case.

DURFEE, Senior Judge, and KUNZIG, Judge, join in the foregoing dissenting opinion.

IN THE UNITED STATES COURT OF CLAIMS

No. 44-68

BETHLEHEM STEEL CORPORATION

v.

THE UNITED STATES

Before DAVIS, Judge, Presiding, DURFEE, Senior Judge, SKELTON, NICHOLS, KASHIWA, KUNZIG and BENNETT, Judges.

ORDER

This case comes before the court on plaintiff's motion, filed March 7, 1975, pursuant to Rule 151 for rehearing and reconsideration of the decision entered herein on February 19, 1975. Upon consideration thereof, together with the response in opposition thereto, without oral argument,

IT IS ORDERED that plaintiff's said motion for rehearing and reconsideration be and the same is denied.

BY THE COURT

Oscar H. Davis

Oscar H. Davis
Judge, Presiding

March 28, 1975

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